Terasen

Growing Value

Annual Report 2004

Growing opportunities

Over the past five years, Terasen has generated value for stakeholders through operational excellence, new project development and expansion of our existing activities. Today we have a solid portfolio of opportunities to ensure our ongoing growth.

Terasen is a leading provider of energy transportation and utility infrastructure management services. We have two strong base businesses—natural gas distribution and petroleum transportation—and an emerging business in water and utility services. Terasen is headquartered in Vancouver, Canada and its shares trade on the Toronto Stock Exchange (symbol: TER).

Contents

Financial highlights

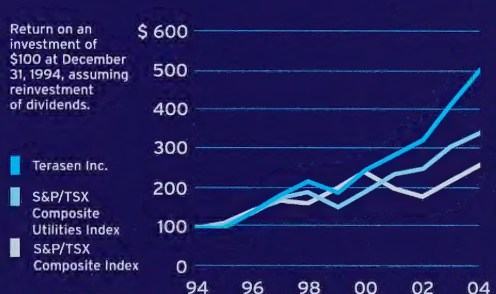
Total shareholder return

Shareholder return including dividends was 19 per cent in 2004. Over the past 10 years, Terasen's annual shareholder return has outperformed both its peer group and the S&P/TSX Composite Index.

Earnings growth

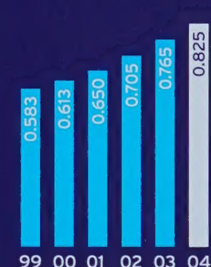
We continue to deliver shareholder value through six per cent annual earnings growth with a corresponding growth in dividends. We are committed to achieving our financial targets while maintaining a low risk profile and focusing on our core businesses.

Shareholder return



Earnings per share
Before non-recurring items
Dollars

Dividends per share
Dollars



Financial results

Dollar amounts in millions except per share data

Years ended December 31	**2004**	2003	2002
Gross revenues	**$ 1,957.0**	$ 1,876.6	$ 1,707.2
Earnings applicable to common shares	**149.8**	132.7	105.8
Operating cash flow	**342.0**	269.8	318.1
Total assets	**4,970.6**	4,921.3	4,522.4
Earnings per share	**1.43**	1.28	1.22
Dividends per share	**0.825**	0.765	0.705
Book value per share	**13.04**	12.51	12.00
Return on common equity	**11.2%**	10.7%	11.7%

Non-recurring items are material gains or losses that, in management's opinion, are not expected to occur on a regular basis. Further explanation of non-recurring items can be found on page 47.

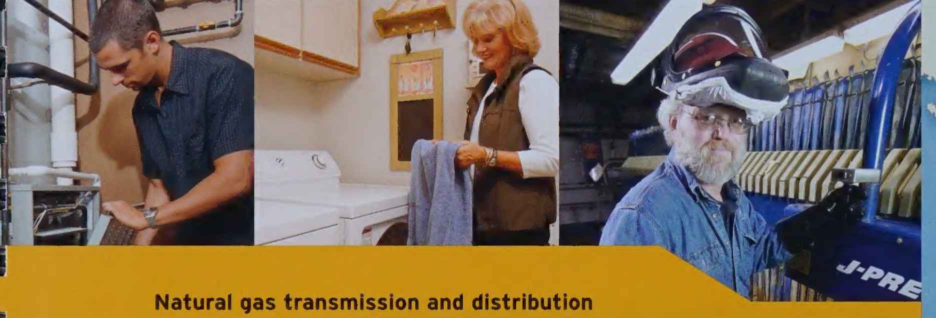
Growth opportunities
across our three businesses

Water and utility services

Growth opportunities of more than $100 million.

Pursue high potential municipal water and sewer projects in Western Canada.

Pursue complementary growth opportunities associated with Fairbanks sewer and water acquisition.



Natural gas transmission and distribution

Vancouver Island LNG Project

Decision anticipated in early 2005. Also potential for additional compression facilities.

Inland Pacific Connector

Proposed gas transmission line connecting Southern Crossing Pipeline to Huntingdon. Likely not required until 2007-2008. Project cost: $300 to $500 million.

Whistler Expansion Project

Potential to replace existing propane system.

Terasen Gas

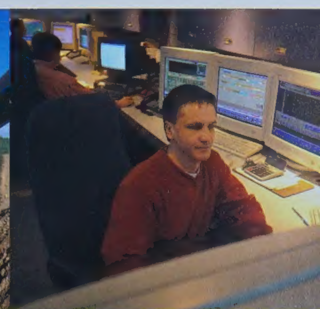
Terasen Gas is the largest distributor of natural gas in British Columbia, serving over 875,000 customers in more than 125 communities. These services are provided primarily by Terasen Gas and Terasen Gas (Vancouver Island). Both companies also operate gas transmission systems.

Terasen Pipelines

Terasen Pipelines is one of the largest petroleum transportation businesses in North America. We own and operate Trans Mountain Pipe Line—which extends from Edmonton to Vancouver and Washington State—and Corridor Pipeline, which extends from the Athabasca oilsands to Edmonton. We also operate and own a one-third interest in the Express and Platte pipeline systems from Alberta to the U.S. Rocky Mountain region and Midwest.

Terasen Water and Utility Services

Terasen Water and Utility Services is the largest private sector provider of water and wastewater products and services in Western Canada. We operate 90 water and wastewater systems in over 50 communities throughout B.C., Alberta and Alaska. We are also a leading operator of outsourced utility services.



Petroleum transportation

Express Expansion Project

Capacity addition of 108,000 barrels per day. Completion in April 2005. Project cost: U.S.$100 million.

TMX Project

Proposed multi-stage expansion providing up to 550,000 bpd of new capacity to either a northern or southern port. The first phase (TMX1) could be fully onstream by late 2008. Total projected cost: $2.2 to $2.6 billion.

Corridor Expansion Project

To meet expansion plans for the Athabasca Oil Sands Project. Involves partial looping of the Corridor Pipeline system. Projected cost: up to $600 million.

Heartland Terminal Project

Proposed tank and cavern storage of 5 to 7 million barrels northeast of Edmonton. Potential in-service date of 2006 with completion by 2010. Projected cost: up to $120 million.

John M. Reid
President and Chief Executive Officer

President's message

At Terasen we are driven by a fundamental commitment to grow value–for our shareholders, for our customers and for the communities where we live and work. Over recent years we have achieved significant success in our endeavours and with a portfolio of well-managed businesses that enjoy outstanding potential for further growth, we are well positioned to sustain this success to the ongoing benefit of all our stakeholders.

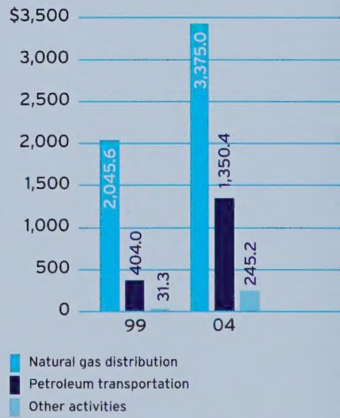
For several years now, the senior management team and I have pursued fulfillment of a very straightforward objective: to consistently deliver low double-digit returns to shareholders through a combination of dividends and earnings growth of at least six per cent per year. I am pleased to report that we achieved this objective in 2004 for the seventh consecutive year.

Terasen's earnings per share for the year increased to $1.43 in 2004 from $1.28 in 2003. In 2004, earnings adjusted to exclude unrealized hedge gains relating to the company's investment in Clean Energy amounted to $1.40 per share, as compared to 2003 earnings of $1.31 per share, adjusted for the impact of a restructuring charge. This represents an increase of 6.9 per cent.

Dividends were increased by 7.8 per cent in April 2004 and the total return to shareholders for the year was 19 per cent. In February 2005 the Board increased the quarterly dividend rate by 7.1 per cent to $0.225 per share.

Advancing the dividend increase from the second to the first quarter better reflects the results of the past year and the prospects for growth in the current year, and ties our dividend payout more effectively to our fiscal year.

Assets
In millions



Assets have more than doubled over the past five years, reflecting completion of value-enhancing projects and acquisitions.

We create shareholder and customer value through operational excellence, consistent financial performance and sustained growth.

Two core businesses and one developing business

Our tight focus on executing the specific measures embodied in our corporate strategy has delivered substantial value for the last several years. As we look to the future and our continuing commitment to our shareholders, our intent is to maintain the tight focus that we have had on our three operating businesses and our critical core competencies. This focus has served us well over the past few years and our potential for future value delivery continues to grow. Natural gas distribution and petroleum transportation are our core businesses and are well established. Our water and utility services business is a developing enterprise which has now grown to a size sufficient to be segregated in our financial reports. All three businesses enjoy prospects for solid growth through new project development, acquisitions and expansion of our existing activities.

Growing with our customers

This is an exciting time to be in the petroleum pipeline business. With the Alberta oilsands undergoing tremendous growth, Western Canadian daily crude production is estimated by the Canadian Association of Petroleum Producers to increase over the next 10 years by 1.1 million barrels, requiring significant growth in pipeline capacity linking production to downstream market refining. In anticipation of this growth, during the past year we have made a concerted effort to better understand and develop effective solutions to meet the needs of producers. Our customer-driven approach to pipeline development is providing positive results, such as the encouraging responses we received to our request for Expressions of Interest in our proposal to develop the TMX project, our ongoing discussions around further pipeline capacity within the oilsands, and the expansion of our Express pipeline system scheduled to come into service in April 2005.

Petroleum transportation capitalizes on the development of the Alberta oilsands

Growing from strength

The current economic resurgence in British Columbia offers very positive prospects for our natural gas utilities. The housing boom in 2004 saw us add more customers to our system than we

Earnings (loss) applicable to common shares
Dollar amounts in millions except per share data

Years ended December 31	2004		2003	
		Per Share		Per Share
Natural gas distribution	$ 95.9	$ 0.92	$ 98.8	$ 0.95
Petroleum transportation	70.9	0.68	56.2	0.54
Water and utility services	6.6	0.06	4.1	0.04
Other activities	(23.6)	(0.23)	(23.0)	(0.22)
Earnings before non-recurring items	149.8	1.43	136.1	1.31
Non-recurring items	–	–	(3.4)	(0.03)
Earnings applicable to common shares	$ 149.8	$ 1.43	$ 132.7	$ 1.28

had in any year in the previous decade. With increased investor confidence, a growing demand for B.C.'s natural resources and a growing provincial population, we anticipate steady growth in our natural gas business both for direct end-user gas consumption markets and in support of new gas-fired generation within the province. Adding to our optimism is a growing interest in developing a regional approach to energy infrastructure planning in the Pacific Northwest, which will support such projects as our proposed Inland Pacific Connector Pipeline.

Growing with our communities

This growing economic activity and the migration of population into Alberta and British Columbia places huge demands on water services at a time when many municipalities are relying on water and wastewater infrastructure developed in the decades prior to the 1970s.

Our water business builds on our utility expertise

Municipal leaders are beginning to recognize the merits of private sector involvement in water and wastewater operations. Reflecting this new reality, in 2004 we entered into agreements to operate the municipal sewer system of the City of Langford on Vancouver Island and to purchase a 50 per cent interest in the water and wastewater treatment and distribution systems of Fairbanks, Alaska. These advances, combined with Terasen's easily transferable expertise in reliable operation of pipeline systems, place us in a strong position to prosper in this developing business. It is our belief that in the future the water segment of our business will come to resemble our natural gas distribution business—a substantial, regulated, low-risk utility.

Investing in our communities

Terasen clearly recognizes that, in addition to economic issues, the long-term viability of our business demands that we sustain a responsible approach in all our endeavours. It is a fundamental principle that social, environmental and safety considerations are critical factors in the decision-making process that guides our activities.

We are committed to supporting strong, vibrant communities in the places where we do business—for both philosophical and practical reasons. We believe strongly in the theory that success breeds success. Successful communities attract new

Terasen is growing value for shareholders through:

Focus
We are focused on low-risk businesses where we can capitalize on our core operating and project management competencies and our geographic strength.

Reliability
We are leveraging our asset management capabilities and strong stakeholder relationships to deliver reliable and consistent results.

Growth
We have substantial growth opportunities compared to the size of our asset base.

capital investment and economic activity. Safe, healthy communities with superior amenities and a high standard of living attract new residents, including skilled workforces. And all of these elements contribute to the ongoing success of our company.

In keeping with this approach, our efforts and investments in community support are highly focused—in the areas of environmental protection and enhancement, education and community development. It is a matter of pride to note that a major aspect of Terasen's community presence is the participation of our employees, individually and in groups.

We focus on the environment, education and community development

Canadians continue to debate the most effective ways to meet Canada's obligations under the Kyoto Accord. Terasen continues to play a leadership role in efforts to manage and reduce greenhouse gas emissions. In 2004, Terasen Gas was awarded gold level reporting status and was named best in industry class by the Voluntary Challenge Registry—the only two-time winner of this award in our industry. Also in 2004, Terasen Pipelines achieved silver level reporting status.

Looking ahead

We enter 2005 poised to continue delivering on our promise of sustained growth and superior value for shareholders. Clearly, we have the necessary asset base and we have significant opportunities. And, even more important, we have highly skilled and committed employees who have played such a central role in Terasen's success to date. In all, the outlook is both encouraging and exciting.

J.M. Reid

John M. Reid
President and Chief Executive Officer
February 17, 2005

Mark L. Cullen
Chairman of the Board

Chairman's message

On behalf of the Board of Directors, I am pleased to report to you and to commend our management team and employees for another year of achievement.

Excellence in governance and ethical standards is the foundation of Terasen's Board and management culture. Within this environment, your Board works together as a team, bringing the skills and experience of our directors to guide, advise and monitor management in the development and execution of strategies to deliver long-term value to shareholders.

For many years we have adopted leading governance practices and we are committed to meeting or exceeding the prevailing benchmarks going forward.

Governance matters were again a strong focus in 2004. We revised our Board and committee mandates to better reflect our responsibilities. We conducted a thorough review of the Board's operational effectiveness and made changes. We reinforced our commitment to keep directors' interests aligned with those of shareholders, by replacing the granting of stock options to directors with deferred share units that cannot be accessed until a director leaves the Board. We also increased minimum share ownership guidelines for directors and senior executives.

Assuring the integrity of our financial statements and controls is paramount. Last year we implemented CEO/CFO certification of financial statements and management continued work to evaluate and improve our internal financial controls systems.

Terasen's growth over the past 10 years has been very gratifying with significant expansion of our gas distribution and oil transportation businesses and the successful development of our water utility business. Over this period, shareholders have enjoyed double digit returns, increasing annual dividends and a record share price. We are proud of our management team and their achievements in creating value for our shareholders.

While we cannot predict the future, we can assure shareholders that the strategic focus for the Board and management remains unchanged: consistent growth in earnings and dividends at relatively low risk given our mostly regulated business environment.

At this year's annual meeting, two of our long-serving directors—Brian Canfield and Dr. David Strangway—will not be standing for re-election. We thank them for their many contributions and counsel and wish them every success in their future endeavours. This year, we welcomed Randolph Aldridge to our Board and we look forward to benefiting from his experience in the U.S. and Canadian oil and gas industry.

Mark L. Cullen
Chairman of the Board
February 17, 2005

We continue to maintain a low-risk profile while pursuing growth opportunities in line with our focus on being a leading provider of energy transportation and utility asset management services.

Growing with our customers

Terasen Pipelines – one of the largest petroleum transportation businesses in North America – is working with customers to deliver growing production from Alberta's oilsands to meet escalating demand in Washington State, California, the U.S. Midwest and Asia.

Production from the Alberta oilsands is growing and shippers and refiners need to move this extra production to California, other parts of the U.S., and Asia. As oilsands production continues to grow, there is increasing demand for petroleum transportation.

Petroleum transportation

We are significantly expanding our petroleum transportation businesses—increasing the capacity of all four pipeline systems: Trans Mountain, Corridor, Express and Platte—and developing a number of other projects. At the same time, we are striving to add value for customers by tailoring these initiatives to accommodate their growing need to transport a variety of petroleum products from production sites to markets.

During 2004, deliveries on our pipeline systems increased substantially over those of the previous year, reflecting higher volumes of crude oil supply from Western Canada and growing demand for oil on the West Coast, the Rocky Mountain states and in the U.S. Midwest. 2004 was also the first full year of operations of the Corridor pipeline.

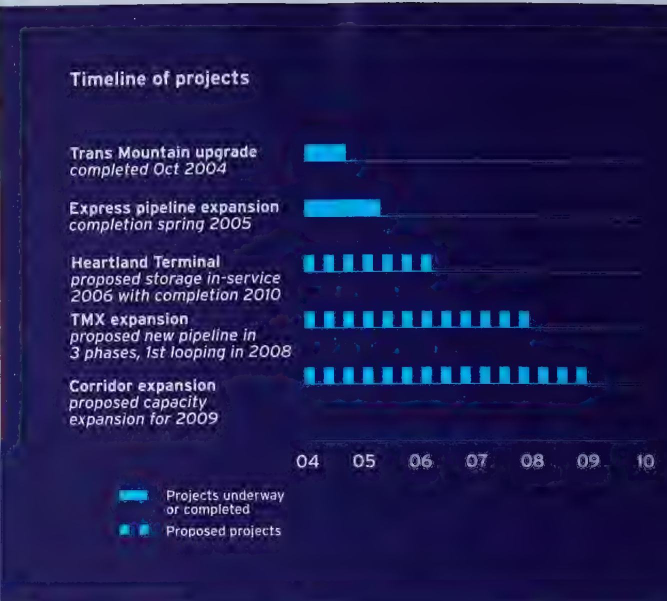
Adding capacity to the Express and Platte pipelines

Our expansion of the Express pipeline will be completed and ready for service in April 2005—on-time and on-budget. This increase is designed to meet the rising demand for petroleum supply to the Rocky Mountain states and to serve the growing delivery needs of Western Canadian producers. The expansion will increase total system capacity to 280,000 barrels per day (bpd) from 172,000 bpd.

We also expect to complete the enhancement of the Platte pipeline capacity by 20,000 bpd between Casper and Guernsey, Wyoming in 2005. This expansion, in conjunction with the added Express capacity, will allow increased deliveries into Denver, Colorado and Wood River, Illinois.

Our goal in any acquisition is to acquire pipeline systems that serve areas of growing demand—and then expand capacity to meet this demand. When Terasen acquired a one-third interest in the Express and Platte pipeline systems two years ago, that was exactly the plan. With this goal achieved, we are actively exploring opportunities to acquire additional pipelines with similar growth potential.

We are increasing the capacity of our four oil pipelines



The TMX project gives shippers the choice of expanding to a northern or southern port, while adding capacity in stages to match growth in supply and demand.

Upgrading the capacity of the Trans Mountain system

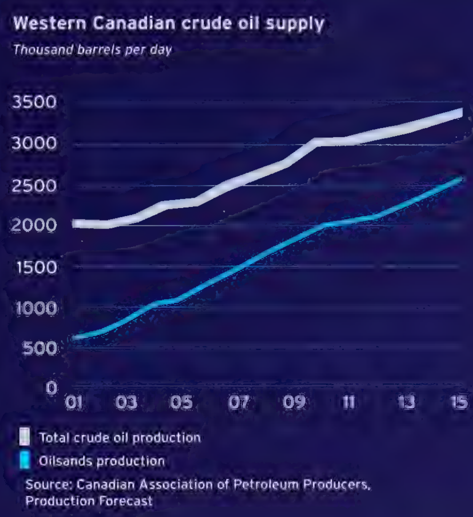
In October 2004, we completed expansion of the Trans Mountain system capacity by 27,000 bpd. As the only petroleum pipeline connecting Alberta to the West Coast, the Trans Mountain system needed this upgrade to meet the increasing demand for Alberta crude oil in Washington State and California.

We're advancing our proposed TMX project

The TMX project is a major expansion along the route of our Trans Mountain system that will enable increased transportation of oil to the West Coast for tanker shipment to markets in California and Asia.

The company was pleased and encouraged by the strong response from a broad range of parties, including existing and new customers, to a TMX Expressions of Interest process which ended in January 2005. Shippers indicated the need for more capacity by 2008, with further expansion by 2010. The next phase of work is to finalize a commercial framework and tolls with prospective shippers and seek formal commitments to TMX in the second quarter of 2005.

The TMX project enjoys several key advantages over competing proposals. First, it can be built in stages, which enables us to add capacity as production grows and markets develop. This reduces risk for customers and the pipeline. Second, because it uses existing transportation corridors, the need for additional land acquisition can be minimized. Third, significant new capacity can be added in the first phase of TMX while preserving the options of expanding through to Vancouver, which would be more attractive for shipments to Washington State or California, or continuing on to



Connecting growing supply to growing demand
As domestic demand in the U.S. continues to outpace domestic production, Terasen Pipelines is actively pursuing the opportunity to link this expanding market with growing output from the Alberta oilsands.

Kitimat or Prince Rupert. A northern port could be preferred if customers intend to ship significant volumes of petroleum to Asia.

Looking ahead to a significant expansion of the Corridor pipeline

We are adding 15,000 bpd of bitumen capacity, along with the required diluent capacity, to the Corridor pipeline by removing bottlenecks on the system. This project will also be completed in 2005.

We are currently working with the Athabasca Oil Sands Project (AOSP) partners on plans for a further major expansion of Corridor within five years. The AOSP partners intend to increase production at their Muskeg River Mine, north of Fort McMurray, and the Corridor pipeline is a key component of this project, connecting the mine to the project's upgrader north of Edmonton.

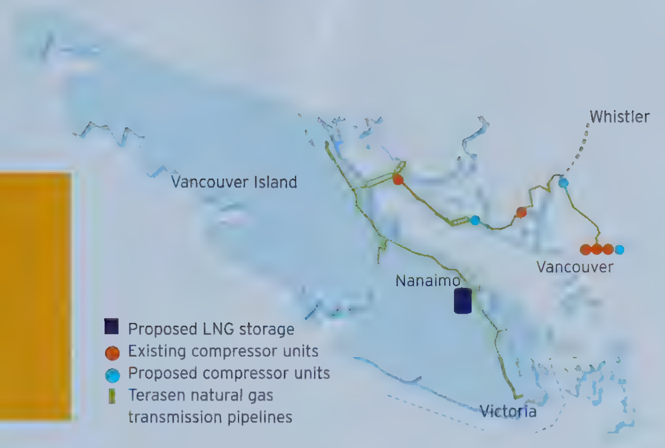
The production growth plans of the AOSP partners will require the construction of a new pipeline to meet their needs. This gives us the opportunity to work with other potential shippers in the oilsands region to meet their needs at the same time. If successful, the Corridor expansion could be integrated with our previously proposed Bison pipeline. This integration would offer many economic and land use benefits, and we are continuing to evaluate its commercial aspects.

Heartland Terminal

Terasen is working with a number of customers on the Heartland Terminal, a proposed new terminal facility northeast of Edmonton near Shell's Scotford Refinery. This project would handle growing oilsands production and provide additional flexibility and product segregation for customers.

Growing from strength

Terasen Gas – the largest natural gas distributor in the Pacific Northwest – is well positioned to participate in providing the gas infrastructure to meet the needs of regional growth – safely, efficiently and reliably.



Terasen is pursuing initiatives to expand capacity to deliver additional natural gas to Vancouver Island, including an LNG storage facility and additional pipeline compression.

Natural gas transmission and distribution

In 2004 we successfully integrated and restructured our mainland, Vancouver Island and Whistler regulated utility operations under a single management team. By increasing efficiencies, using common technology platforms and integrating key business processes, we have created a foundation of expertise that is transferable to other acquisition opportunities.

Our success has resulted in reduced operating costs, including lower costs to connect new customers. At the same time, we have met or surpassed the service quality indicators required for safety, cost, customer satisfaction and environmental responsibility under performance-based regulation. In particular, we achieved significant improvement in satisfaction among builders and developers, a group vitally important to increasing market capture. We achieved these improvements largely through the hard work and focused performance of our employees, who faced the significant challenges created by a substantial increase in new housing construction.

Increasing our customer base

We added almost 16,000 new customers in 2004, reflecting stronger economic growth in B.C., particularly in Greater Vancouver and the Okanagan. We now have over 875,000 customers throughout the province, and we set a new goal to have one million customers by 2010.

Increasing market share of natural gas in new construction

We intend to increase our share of the market for natural gas in new multi-family housing developments, which make up about 60 per cent of the residential construction market in British Columbia. To better access and serve this market, we are streamlining our processes with builders and developers, and we have created key account contacts to make it easier for major developers to work with us. As space efficiency is a key consideration in high-rise multi-family developments, we are also working to have small gas meters available in order to provide for individual metering for each unit.

A leader in operating efficiency
In addition to delivering outstanding safety and reliability, our long-term focus on performance excellence has made Terasen's natural gas distibution segment an industry leader in operational efficiency. The number of customers per employee is the highest in the industry, while costs associated with operating and maintenance and net plant investment per customer are among the lowest in the industry.

Other ways to increase our customer base to one million by 2010 include working with BC Hydro on demand-side management and partnering with communities to assess how we can best serve them in the future.

Expanding capacity to Vancouver Island

We are advancing plans to build a liquefied natural gas (LNG) facility southwest of Nanaimo which—together with expansion of compression capacity to Vancouver Island—will serve to strengthen the reliability of gas supply for customers on Vancouver Island. The LNG plant will enable storage of natural gas near major centres, in keeping with B.C.'s energy policy, while the overall increase in gas capacity will help fuel the additional electricity generation needed to meet demand.

In 2004 the Cowichan Regional District issued siting and rezoning approval for the LNG project, as well as general expressions of support. The facility is targeted for completion in the summer of 2007.

Helping Whistler meet its energy infrastructure needs

Whistler is a growing community and as it prepares for the 2010 Winter Olympics, energy infrastructure management is key. The municipality is nearing capacity of our existing propane plant and we are working closely with Whistler to determine future energy requirements for housing, recreation and transit. Options being explored range from a new gas pipeline to Whistler, centralized energy infrastructure to ground source heat pumps. The community is expected to make its decision on long-term energy infrastructure by mid-2005.

Inland Pacific Connector

Terasen Gas is taking a leadership role in regional demand/supply planning for British Columbia and the Pacific Northwest region. Along with major load-serving organizations, such as gas distribution companies and electricity companies with gas-fired generators, we recently collaborated on a study that assessed future demand growth for natural gas in the Pacific Northwest.

A growing population and ever-increasing demand for electricity is a challenge for British Columbia, especially Vancouver Island. Helping customers switch to high-efficiency natural gas heating systems will reduce demand, ensuring the most energy-efficient fuel is used for home heating.

Terasen Gas embarked on a series of programs throughout 2004 to raise consumer awareness about energy efficiency. Special offers encouraged consumers to convert to home-heating systems carrying the ENERGY STAR® label, and were made possible with cooperation from Natural Resources Canada, BC Hydro and various equipment manufacturers.

Homeowners were offered up to $1,350 in rebates when they converted to energy-efficient natural gas appliances. As a result, Terasen Gas was recognized as a leader in the promotion of energy efficiency, winning the 2004 Industry Advocate Award from Natural Resources Canada.

The report, published in the summer of 2004, determined that significant capacity expansion will be needed by 2008 to meet growing demand.

We have completed the first phase of the provincially led environmental review process on our proposed Inland Pacific Connector Pipeline project. With the proposed LNG storage facility and the preparatory work done on the Inland Pacific Connector, we are well positioned to respond to the marketplace as demand for natural gas grows.

In 2004, Terasen Gas helped roll out a program for small business owners called Natural Gas Unbundling, which separates the natural gas commodity from delivery costs. Under this program, small businesses can choose to buy natural gas from independent gas marketers who offer contracts for the natural gas commodity at a fixed price for a fixed period of time, ranging from one to five years. Terasen continues to deliver the gas and look after all billing and service functions. Approximately 10 per cent of our commercial customers opted for this program. We also introduced a Stable Rate Option for residential customers who wish to lock in the commodity price of natural gas for one year. One of the aims of this trial program is to educate customers about the cost and pricing of natural gas, while ensuring that the risks of offering a fixed rate to customers are appropriately managed.

More choice for customers when buying natural gas

Our ongoing gas purchasing strategy strives to keep the cost of gas for our customers as low as possible, dampens price volatility and helps to ensure that our rates remain competitive with consumer costs for electricity in B.C., which are among the lowest in North America. The cost of natural gas, which flows directly through to the consumer, makes up roughly two-thirds of a residential customer's bill.

Growing with our communities

Terasen Water and Utility Services is working closely with communities to meet their needs for reliable and cost-effective water and energy systems and related utility management services.

Terasen is the largest private sector provider of water and wastewater products and services in Western Canada. We operate 90 water and wastewater systems in over 50 communities throughout B.C., Alberta and Alaska.

Water and utility services

We continue to build our water business by offering municipalities a full range of water and wastewater treatment and distribution products, systems and services. This market features outstanding potential for ongoing growth as communities everywhere face the need to upgrade infrastructure and invest in new technology to meet increasingly high standards for water and effluent quality.

To expand our established position in Alberta and British Columbia we are targeting small to medium-sized municipalities whose existing water and sewage infrastructures need major expansion to keep pace with population growth. For example, in 2004 we began operating the municipal sewer system for the City of Langford on Vancouver Island under a long-term contract, and we will own expansions to the sewer system. Elsewhere, similar arrangements enable other communities to benefit from our expertise, experience and investment strengths. We also provide water metering operations in a number of locations in Canada and the United States.

Our broad range of capabilities enables us to develop long-term relationships with municipalities—often starting by providing water infrastructure products or meter installations and services. We then gain a deeper understanding of the community's needs, and are able to offer solutions through additional services in utility infrastructure and management.

We are developing long-term relationships with municipalities

During 2004 we acquired a 50 per cent interest in Fairbanks Sewer and Water in Alaska—an operation that we believe provides an example of how our business will be run in the future. It is a privately held company that supplies comprehensive water and wastewater treatment and distribution services to the City of Fairbanks, a community of 82,000 residents, and it operates under the jurisdiction of the Regulatory Commission of Alaska. We anticipate that many, if not all, water systems will eventually come under regulatory oversight similar to the structures governing natural gas and electricity operations.

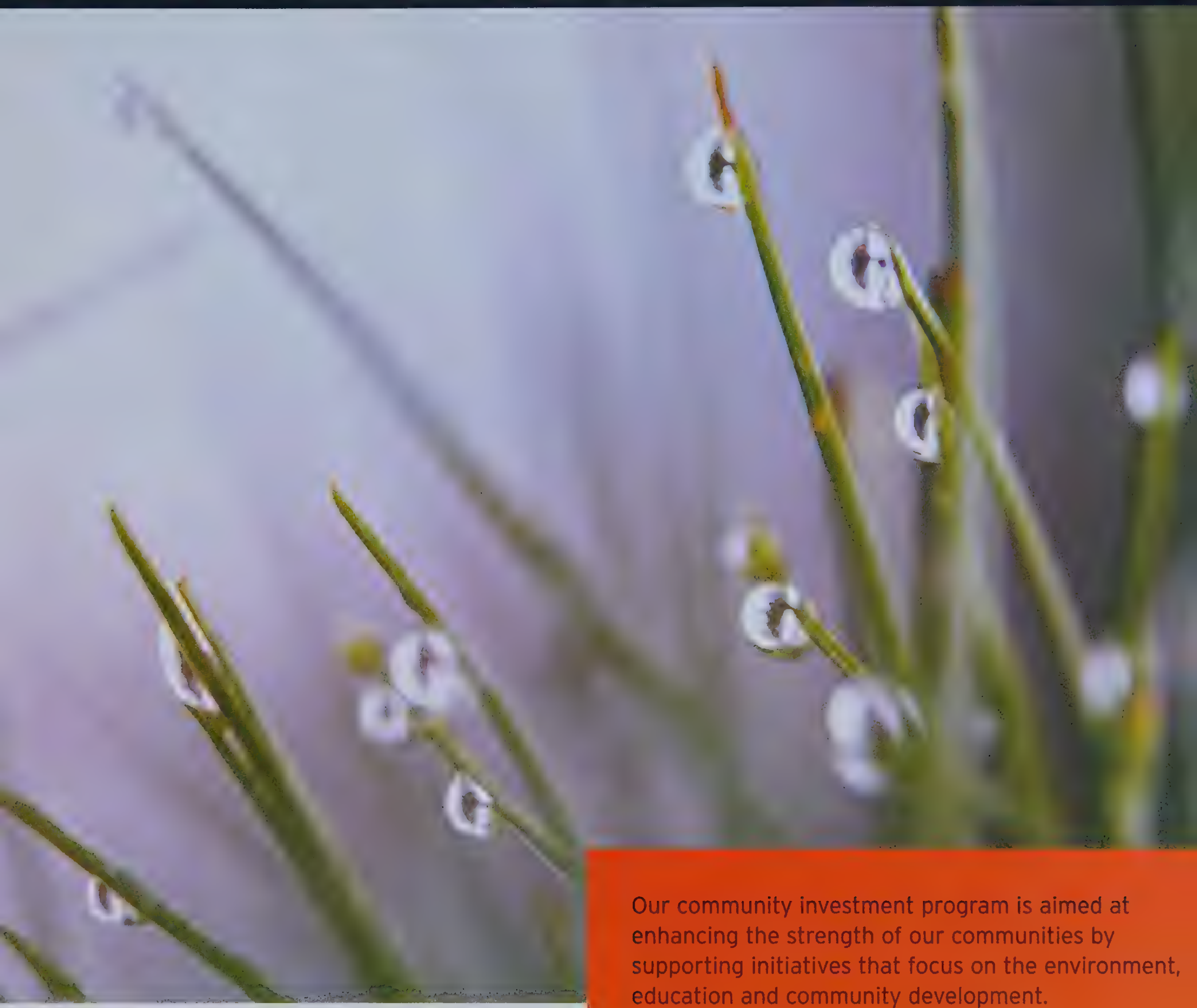
Investing in our communities

Strong societies thrive on dedication and shared purpose. We are committed to actively working in partnerships that enhance the vitality and long-term sustainability of the communities where we operate.

Reducing greenhouse gas emissions
In 2004, for the sixth consecutive year, Terasen Gas was awarded gold level reporting status from the Voluntary Challenge and Registry (VCR), reflecting our efforts to manage greenhouse gas emissions. We also earned the VCR's leadership award for our industry sector—the only company in this sector to receive this award twice.

These honours acknowledge our initiative in setting reduction targets and taking specific actions to achieve them. In 2004, Terasen Gas voluntarily set a more challenging standard for its efforts, establishing year 2000 emission levels as its new baseline for comparing and reporting current year performance. Previous submissions used a 1990 emissions baseline for comparison. For the most current reporting period, operating emissions were five per cent below 2000 levels—and down a total of 14 per cent after accounting for offset project reductions. The role of the VCR was recently incorporated into the Canadian Standards Association (CSA). Terasen Gas plans to continue in the program under the CSA.

Terasen Pipelines achieved VCR silver level reporting status in 2004 and 2003 and has registered to take part in the American Petroleum Institute Climate Change Program.

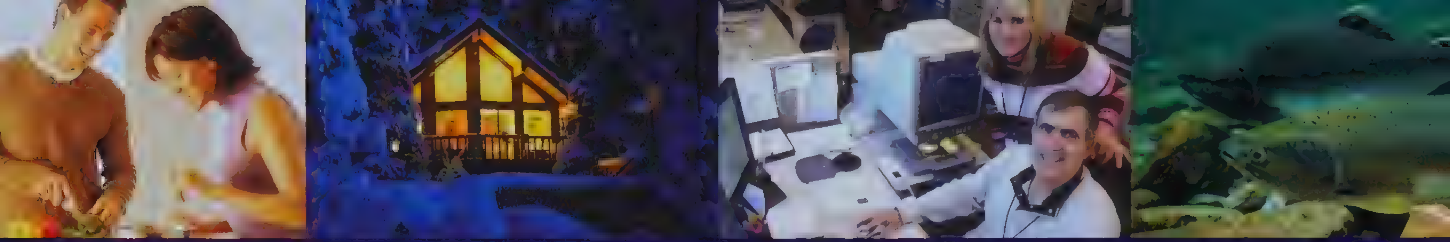


Our community investment program is aimed at enhancing the strength of our communities by supporting initiatives that focus on the environment, education and community development.

Environmental Community Outreach
Terasen's focus on supporting clean air and water is reflected in our Environmental Community Outreach (ECO) program, which since its start in 1999 has contributed to the success of a number of fish and wildlife habitat enhancement projects on Vancouver Island. The program was expanded in 2004 to include projects in the Greater Vancouver area.

In partnership with Douglas College's Institute of Urban Ecology, ECO completed its first Vancouver area project in early December, aiding the Institute's Green Links program. Green Links creates ecological links between wildlife habitats by increasing the amount of native vegetation in sensitive areas. For this project Terasen employee volunteers removed invasive plant species, cleaned up sites to prepare them for planting and installed bird boxes along a stream in Surrey.

Reducing water consumption
In a program aimed to help communities reduce water consumption, in 2004 Terasen designed and managed successful volunteer water metering projects in Kamloops and Surrey. In the program, residents volunteer to have their water consumption monitored by meters installed by Terasen.



Education

Support for education is a key thrust of our commitment to strong communities, with a particular focus on training in engineering, sciences and trades. In 2004, Terasen provided bursaries for students at 26 post-secondary institutions along our petroleum pipeline routes in Canada and the United States—including eight new bursaries at U.S. schools along the routes of the Express and Platte systems.

In keeping with our interest in supporting strong First Nations communities in B.C., Terasen established an endowment at Vancouver Community College in 2004, aimed at helping Aboriginal students to upgrade their skills and go on to university. Terasen is also the lead sponsor of the Chinook Program at the University of British Columbia's Sauder School of Business. This program offers First Nations students certificate, diploma and undergraduate education in management, training future Aboriginal leaders in the practices of commerce and industry. We are working with other B.C. companies to increase support for the Chinook program.

Employee-led giving programs

In 2004, Warm Hearts, a program developed and managed by Terasen Gas employees to support health and well-being in the communities where they live and work, celebrated its 10th anniversary. Since the program's start in 1994, employees have donated $341,000 to more than 44 charitable organizations throughout British Columbia.

Terasen employees make a difference

Terasen employees are long-standing supporters of the United Way. Our fundraising campaigns surpassed their goals in 2004 and focused on increasing involvement by employees and retirees.

Creating partnerships with Aboriginal communities

For a number of years, Terasen has been building mutually beneficial working relationships with First Nations groups. Our efforts acknowledge the fact that Aboriginal bands are increasingly significant landowners in areas where we operate. In 2004, the company adopted a

Terasen supports Calgary's 'Forever Green' program, dedicated to expanding the city's urban forest. In September 2004, company employees, family members and friends planted over 200 seedlings at a popular riverside park. This complements our ongoing support of the Tree Canada initiative, which encourages community tree planting and tending to combat CO_2 emissions.

formal Statement of Principles for Aboriginal relations, spelling out our commitment to conduct business in a manner that respects the social, economic and cultural interests and expectations of First Nations communities.

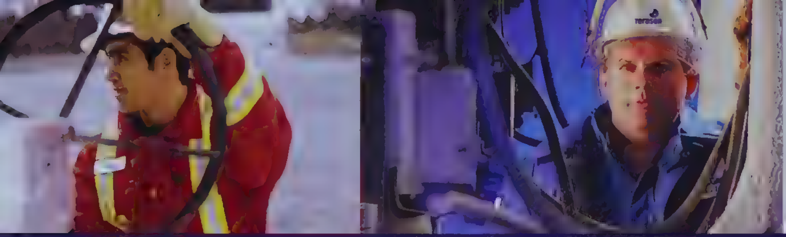
Terasen has formal, written agreements and memorandums of understanding with a number of Aboriginal bands, including a long-term contractual arrangement with the Cowichan on eastern Vancouver Island. Several more agreements are currently in process. In 2004, Terasen Utility Services signed a major memorandum of understanding with the Kamloops Indian Band—the largest the company has established with a First Nations community. Terasen Utility Services will be working with the Kamloops Indian Band to develop industrial, commercial and residential land that can't be connected to the existing sewage system. The proposed development will provide a new sewer infrastructure, sewage treatment and other utility services on band land. Benefits to the band community include job and training prospects, as well as opportunities for further property and business development.

Our Aboriginal partnerships generate opportunities

Consulting with our stakeholders

A number of activities during 2004 reflected our commitment to consultation with community stakeholders who provided valuable input into our major project planning processes. On Vancouver Island, we conducted public consultation sessions to discuss our proposal to build a liquefied natural gas facility. The process enabled us to gain public support for siting of the proposed facility.

In preparation for our proposed TMX pipeline project, we have started discussions with Aboriginal groups, held a workshop with key Western Canadian environmental organizations and have begun to contact landowners and residents located in close proximity to project activities.



Natural gas division improves safety record
Terasen Gas has reduced the frequency of lost time injuries and recordable vehicle accidents in its operations, reflecting a sustained emphasis on improving employee safety.

Frequency of Lost Time Injuries

2000	2001	2002	2003*	2004*
1.76	2.13	1.81	1.27	1.11

Frequency of lost time injuries is measured by the number of incidents per 200,000 hours worked.

Frequency of Recordable Vehicle Accidents

2000	2001	2002	2003*	2004*
4.71	4.64	4.07	3.61	3.44

Frequency of recordable vehicle accidents is measured by the number of accidents per million kilometres driven.

*Includes Terasen Gas Vancouver Island

Lower Lonsdale Energy Corporation

An innovative heating system developed and implemented by Terasen Utility Services in partnership with the City of North Vancouver won three major awards in 2004, including a national Energy Efficiency Award for outstanding development and promotion of energy efficiency. The Lower Lonsdale energy project involves an interconnected system of mini plants, installed in new and existing buildings and using high-efficiency boilers. Combined, they generate as much heat energy as one large plant can, but more efficiently and cost-effectively.

Innovative project wins national energy efficiency award

Approximately three million square feet of new residential and commercial space is being redeveloped in North Vancouver's Lonsdale area. Because of advance planning, the mini heating plants can be installed cost-effectively in new construction. The first mini plant is complete and the second will be completed in mid-2005. Terasen Utility Services will be able to apply this new efficient energy expertise in future high-density residential and commercial developments.

Educating the public about safety

Public safety is fundamental to our business

This year, Terasen joined with the Propane Gas Association of Canada to create a propane gas safety brochure. Terasen Gas previously developed components of the B.C. Fire Services curriculum *Getting to Know Fire* in an attempt to increase the public's understanding of gas safety and emergency preparedness.

In 2004, Terasen provided funding to 32 rural, county and city fire departments that provide first response to any emergency along the oil pipeline from the Canadian border to Wood River, Illinois.

The pipelines division formalized an Integrated Public Awareness Program,

The positive response we receive from communities when we develop major projects reflects Terasen's commitment to doing business in a responsible and respectful manner. This community approval rating is a valuable asset when seeking support for future initiatives.

designed to educate members of our communities on issues such as pipeline damage prevention and effective emergency response, as well as informing them about ongoing maintenance projects. The public plays an important role in helping to prevent pipeline emergencies resulting from third-party damage and right-of-way encroachment.

Community investment funding applications now on-line

Community groups can now apply for funding from Terasen's community investment program faster and easier through a new on-line application process.

Applications and selection criteria are available at:

www.terasen.com
www.terasengas.com
www.terasenpipelines.com
www.terasenwaterworks.com
www.terasenutilityservices.com

MD&A at a Glance

This discussion should be read in conjunction with the consolidated financial statements of the Company and related notes for the years ended December 31, 2004 and 2003. In this MD&A, we, us, our, the Company and Terasen mean Terasen Inc., its subsidiaries, joint ventures and investments in significantly influenced companies. Terasen Gas refers to Terasen Gas Inc., TGVI refers to Terasen Gas (Vancouver Island) Inc., Trans Mountain refers to Terasen Pipelines (Trans Mountain) Inc., Corridor refers to Terasen Pipelines (Corridor) Inc., Terasen Pipelines refers to Terasen Pipelines Inc., Express refers to the Express and Platte Pipeline Systems; and Water and Utility Services refers to Terasen Waterworks (Supply) Inc., Terasen Utility Services Inc., Terasen's 50% interest in Fairbanks Sewer and Water Inc. and Terasen's 30% interest in CustomerWorks LP.

Performance Highlights - provides an overview of the financial and operational achievements of 2004 and a look ahead at the opportunities for 2005.

About Terasen - describes Terasen's vision, core businesses and strategy.

Key Risk and Success Factors - discusses key factors influencing the Company's financial and operating performance and the risk management activities designed to mitigate the risks associated with the key success factors.

Financial and Capital Management - provides a detailed discussion of how we manage our financial and capital resources.

Financial Results - provides a comparative review of the financial performance for the consolidated Company over the past two years. It also provides an analysis of the performance of the separate business units.

Business Development - reviews the Company's activities with regard to system expansions and growth by acquisition.

Critical Accounting Policies and Estimates - provides a summary of the critical accounting policies and estimates used in the preparation of the Company's consolidated financial statements.

Review of 2004

Earnings Growth – In 2004, Terasen reported earnings of $149.8 million, an increase of $17.1 million over earnings of $132.7 million in 2003. On a per share basis, earnings increased to $1.43 per share in 2004, compared with $1.28 per share in 2003. Included in 2004 earnings was a $3.3 million gain arising from Clean Energy's price risk management activities. Excluding the gain, Terasen's earnings were $146.5 million, or $1.40 per share, up 6.9% over 2003 earnings per share before non-recurring items of $1.31.

Dividend Increase and Stock Split – On April 22, 2004, Terasen's Board of Directors approved a 7.8% increase in Terasen's quarterly cash dividend and a two-for-one stock split of the Company's common shares outstanding. All per share amounts have been restated to reflect the two-for-one stock split, which took effect on June 7, 2004.

Natural Gas Distribution – Achieved operating efficiencies between Terasen's mainland and Vancouver Island natural gas utilities, which were shared between shareholders and customers, and offset the impact of the lower allowed return on equity.

Trans Mountain Expansion – An upgrade of the Trans Mountain pipeline which increased capacity by 27,000 barrels per day (bpd) was completed in 2004.

Express Pipeline Expansion – Construction commenced on an expansion on the Express Pipeline System, which will provide an additional 108,000 bpd of capacity and is expected to be completed by April 2005.

Fairbanks Acquisition – In 2004, Terasen acquired a 50 per cent interest in Fairbanks Sewer and Water Inc. (FSW). FSW provides water and wastewater treatment and water distribution and wastewater collection services to Fairbanks, Alaska, an area of 82,000 residents.

Performance Highlights

EARNINGS (LOSS) APPLICABLE TO COMMON SHARES[1]

Years ended December 31	**2004**		2003		2002	
In millions of dollars except per share amounts		**Per Share**		Per Share		Per Share
Natural gas distribution						
Terasen Gas	**$ 69.7**	**$ 0.67**	$ 72.6	$ 0.70	$ 69.5	$ 0.80
TGVI	**26.2**	**0.25**	26.2	0.25	22.9	0.27
	95.9	**0.92**	98.8	0.95	92.4	1.07
Petroleum transportation						
Trans Mountain	**39.4**	**0.38**	35.8	0.35	29.3	0.34
Corridor	**15.6**	**0.15**	10.7	0.10	—	—
Express System	**15.9**	**0.15**	9.7	0.09	—	—
	70.9	**0.68**	56.2	0.54	29.3	0.34
Water and utility services	**6.6**	**0.06**	4.1	0.04	0.9	0.01
Other activities	**(23.6)**	**(0.23)**	(23.0)	(0.22)	(16.8)	(0.20)
Earnings before non-recurring items	**149.8**	**1.43**	136.1	1.31	105.8	1.22
Non-recurring items[2]	**—**	**—**	(3.4)	(0.03)	—	—
Earnings applicable to common shares	**$ 149.8**	**$ 1.43**	$ 132.7	$ 1.28	$ 105.8	$ 1.22

[1] *All per share amounts have been restated to reflect the two-for-one stock split, which took effect in June 2004.*
[2] *Non-recurring items is a non-GAAP measure which is described in detail in the section "Non-GAAP measures".*

Outlook for 2005

ABOUT TERASEN

VISION

Terasen's vision is to be a leading provider of energy transportation and utility asset management services. Our vision is characterized by the pursuit of operational excellence at all times, with a commitment to providing consistent and steady financial performance. Terasen's competency is the provision of operating services associated with gas distribution, petroleum transportation, and water and wastewater distribution. We have developed an asset management concept, which can employ financial partners and high quality service providers to optimize the cost of capital and deliver operating efficiencies both with existing operations and potential acquisitions. In the role of asset manager, the Company creates shareholder and customer value by leveraging a combination of operational excellence, financial excellence and focused business development.

Operational Excellence

The strength of Terasen's business is its ability to operate physical assets for the benefit of customers. Given the regulated nature of Terasen's core businesses, the Company can create value through incentive regulatory arrangements that allow Terasen to share with customers the benefits of cost efficiencies and reliable customer service. To capitalize on these opportunities, Terasen is focused on achieving operational excellence through strong performance in system reliability, cost management, customer satisfaction, safety and environmental responsibility.

Financial Excellence

Terasen's low-risk business profile has been achieved through a variety of means, including a focus on growth in regulated businesses, disciplined capital investment criteria in non-regulated businesses, maintenance of sound regulatory constructs such as deferral accounts, risk mitigation through long-term contracts and a strategic focus on complementary assets and geographical locations. Terasen's low-risk profile has enabled it to achieve a cost-efficient capital structure and reliable access to capital markets. In addition, the Company has developed relationships with financial partners who can provide access to cost-effective pools of capital.

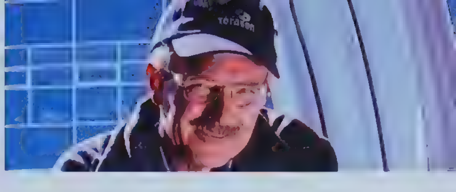
Focused Business Development

Terasen can create value through the development of new infrastructure projects, greenfield expansions and selective acquisitions. This includes securing commitments from customers to reduce the risk profile of investments, and managing construction risk to complete projects on time and on budget. Terasen also pursues selective acquisitions where there is the opportunity for value creation; where the Company can reduce costs or increase revenues through integration with existing operations, where a cost of capital reduction can be achieved, or where there is opportunity for post-acquisition expansion. The Company has also created value by growing its non-regulated businesses that have been developed from Terasen's core competencies of safe, efficient and reliable operation of distribution systems.

CORE BUSINESSES

Natural Gas Distribution

Terasen's natural gas distribution operations consist primarily of Terasen Gas and TGVI in addition to several small related utility operations. Terasen Gas is the largest distributor of natural gas in British Columbia, serving more than 792,000 customers in more than 100 communities. Major areas served by Terasen Gas are Greater Vancouver, the Fraser Valley and the Thompson, Okanagan, Kootenay and North Central Interior regions of the



province. TGVI serves approximately 81,000 customers on Vancouver Island and the Sunshine Coast area and Terasen Gas (Whistler) serves approximately 2,000 customers in the Whistler region. Terasen Gas and TGVI provide transmission and distribution services to their customers, and obtain natural gas supplies on behalf of residential and commercial customers. Gas supplies are sourced primarily from northeastern British Columbia and from Alberta, through Terasen's Southern Crossing Pipeline.

Petroleum Transportation

Terasen's petroleum transportation operations are the Trans Mountain, Corridor, Express and Platte pipelines. Trans Mountain transports crude oil and refined products from Edmonton, Alberta to Burnaby, British Columbia and also delivers Canadian crude oil to several refineries in Washington State. Trans Mountain also owns the Westridge Marine Terminal, which is located at tidewater in the Port of Vancouver, and a jet fuel pipeline connecting to Vancouver International Airport. Corridor owns a dual pipeline system which transports diluted bitumen and diluent between the Muskeg River mine near Fort McMurray and the Shell upgrader north of Edmonton, Alberta. Corridor commenced commercial operations in May 2003. Terasen also owns a one-third interest in the Express Pipeline and the Platte Pipeline which transports crude oil from Hardisty, Alberta to the Rocky Mountain region of the United States and on to Wood River, Illinois.

Water and Utility Services

Terasen's water and utility services operations include Terasen Waterworks, Terasen Utility Services, Terasen's 50% interest in Fairbanks Sewer & Water and Terasen's 30% interest in CustomerWorks LP. Terasen Waterworks provides water and wastewater infrastructure products and services primarily in Western Canada. Terasen Utility Services is a provider of outsourced utility services, operating over 90 systems in more than 50 communities, as well as several other utility contracts throughout North America. CustomerWorks provides billing and customer care services for almost 2.6 million customers to utilities, municipalities and retail energy companies. CustomerWorks has outsourced the provision of its customer care services to an entity owned and operated by Accenture Inc.

STRATEGY

Terasen's core competencies are in the management and operation of infrastructure assets, in particular transmission and distribution utilities and petroleum pipelines. Our strategy is designed to take advantage of these competencies and create value by applying these competencies and skills to a larger asset base. Growth in assets is expected through a combination of organic growth, greenfield expansions and accretive merger or acquisition opportunities.

Natural Gas Transmission and Distribution

Near term growth opportunities for Terasen's natural gas transmission and distribution business will be to focus on increasing new customer capture rates and maintaining the efficiencies achieved through the operational integration of Terasen Gas and TGVI. Through programs and activities designed to deliver operational excellence together with incentivized regulatory arrangements, Terasen derives value from its natural gas transmission and distribution assets. The Company's long term growth objective for its natural gas distribution business is to capitalize on its operating competencies by combining additional transmission and distribution assets with its existing asset base. The competencies applicable to natural gas distribution are also applicable to electricity distribution and water distribution.

Petroleum Transportation

Terasen's key strategic objective for its petroleum transportation business continues to be to respond to the transportation needs of crude oil and refined products shippers and capitalize on the growth opportunities arising from the Alberta oilsands. The expected growth of bitumen and synthetic crude oil production in Alberta will require additional pipeline capacity, both to move production to the Alberta pipeline hubs, and to move production from Alberta to downstream markets in Western Canada, the United States and offshore. The value of existing Trans Mountain pipeline assets continues to be enhanced through strong throughput, incentive regulation, and continuing delivery of operational excellence.

Expansion initiatives in support of this strategy include the capacity upgrade completed in 2004, the current expansion of the Express System and the development of TMX and the Bison Pipeline. The Company is working closely with shippers to address their needs for pipeline capacity and actively developing the right pipeline solutions to provide value for both our shippers and shareholders.

Water and Utility Services

Terasen's water and utility services business is positioned as Western Canada's private sector market leader in the provision of water and wastewater infrastructure products and services and is a primary operator for outsourced utility services. The water and utility services business strategy is to lever off the core competencies and processes of Terasen's existing businesses and provide efficient and flexible solutions at all points along the water distribution value chain. Its operations include the design, build and operation of water and wastewater treatment plants and distribution/collection systems, the supply of products, as well as the provision of outsourced utility services. The primary market for Terasen water and utility services is growing municipalities with significant needs for water and utility infrastructure that are looking for opportunities to lower their cost of providing these services.

KEY RISK AND SUCCESS FACTORS

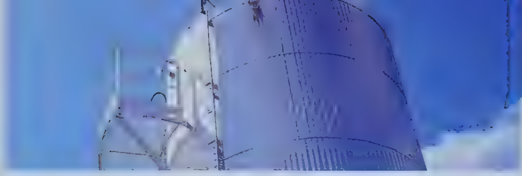
Terasen's operating and financial performance is influenced by a number of success factors which include, but are not limited to, the following:

- Appropriate regulatory arrangements
- Appropriate risk management and governance processes
- Safe, reliable and efficient asset management processes
- Focused business development activities
- Energy market conditions
- Ready access to capital markets

The following is a discussion of these success factors and the activities Terasen undertakes to mitigate associated risks.

REGULATORY ARRANGEMENTS

Regulated businesses represented 96% of Terasen's asset base at December 31, 2004. Accordingly, it is essential that Terasen maintain good relationships with its various regulators and customer representatives. Appropriate, incentivized regulatory arrangements provide Terasen's regulated businesses with an opportunity to manage costs and service quality, resulting in a sharing of benefits between customers and shareholders. Through the regulatory process, the British Columbia Utilities



Commission (BCUC) approves the return on equity which Terasen Gas and TGVI are allowed to earn, in addition to various other aspects of utility operations. Fair regulatory treatment that allows Terasen Gas and TGVI to earn a risk adjusted rate of return comparable to that available on alternative, similar investments is essential for ongoing capital attraction and growth.

Trans Mountain is in discussions with shippers regarding the commercial terms for a new Incentive Toll Settlement (ITS) to replace the current ITS which is set to expire at the end of 2005. Terasen's other businesses also have in place a number of performance based regulatory frameworks which provide for additional returns based on operating efficiencies. There is a risk that upon expiry of existing agreements, new agreements may not provide the same opportunities for returns from efficiencies that exist today.

Regulation – Terasen Gas

Terasen Gas is regulated by the BCUC, which approves rates for services and issues certificates for the construction of major facilities. Traditionally, rates have been set using the cost of service approach to utility regulation. Since 1996, however, incentive-based regulation has been used in the rate-setting process in order to enhance value to customers and provide opportunities for enhanced returns to shareholders.

Rate Deferral Accruals

Terasen Gas' rates are based on estimates of several items, such as natural gas sales volumes, cost of natural gas, and interest rates. In order to manage the risks associated with some of these estimates, a number of regulatory deferral accounts are in place.

Two mechanisms to ameliorate unanticipated changes in sales volumes, such as changes caused by weather, have been implemented specifically for Terasen Gas. The first, originally called the Gas Cost Reconciliation Account (GCRA), relates to the recovery of all gas costs through a deferral account which captures all variances (overages and shortfalls) from forecasts. Balances are either refunded to or recovered from customers via an application with the BCUC. Creation of the GCRA was approved by the BCUC in October 1993; effective April 2004 the GCRA was split into two new deferral accounts called the Commodity Cost Reconciliation Account (CCRA) and the Midstream Cost Reconciliation Account (MCRA). The CCRA and MCRA were created to support commodity unbundling and the refund/recovery mechanism works the same as that used for the GCRA. The second mechanism seeks to stabilize revenues from residential and commercial customers through a deferral account that captures variances in the forecast versus actual customer use throughout the year. This mechanism is called the Revenue Stabilization Adjustment Mechanism (RSAM).

The RSAM and CCRA/MCRA accounts reduce Terasen Gas' earnings exposure to related risks by deferring any variances between projected and actual gas consumption and gas costs, and refunding or recovering those variances in rates in subsequent periods. Variances in usage by large volume, industrial transportation and sales customers are not covered by these deferral accounts as their usage is more predictable and less likely to be significantly affected by weather.

Recovery of the deferral account balances in rates charged to customers led to a decline in the regulatory deferral accounts during the year. In 2004, the net balances of the RSAM and CCRA/MCRA accounts declined to $14.1 million from $38.5 million in 2003.

In order to ensure that the balances in the CCRA/MCRA account are recovered on a timely basis, Terasen Gas prepares quarterly calculations to determine whether customer rate adjustments are needed to reflect prevailing market prices for natural gas costs.

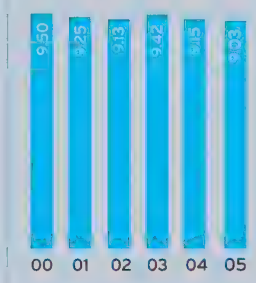
Short-term and long-term interest rate deferral accounts are also in place to absorb interest rate fluctuations. The interest rate deferral accounts which were in place during 2004 effectively fixed the interest expense on short-term funds attributable to Terasen Gas' regulated assets at 3.25% during 2004. The effective fixed short-term interest rate for 2005 has been set at 4.00%. Any variations from this rate throughout the year are recorded in deferral accounts.

The Company's pension obligations are funded by pension plan investments in a variety of assets, including equities, where investment returns may be insufficient to meet pension obligation liabilities. The majority of the Company's pension obligations relate to regulated businesses, where pension deficits are generally recoverable through the regulatory process. As part of the 2004-2007 Performance Based Rate Plan (PBR) settlement for Terasen Gas, a new deferral account was established for pension costs. In addition, the PBR settlement set forth a new deferral account for insurance premiums, which had not been included in previous regulatory settlements.

Allowed Return on Equity (ROE)

Terasen Gas' allowed ROE is determined annually based on a formula that applies a risk premium to a forecast of long-term Government of Canada bond yields. For 2005, the application of the ROE formula set Terasen Gas' allowed ROE at 9.03%, down from 9.15% in 2004. The ROE reduction reflects lower forecasted long-term bond yields for 2005, compared to those used in the 2004 ROE calculation.

Terasen Gas Inc.
Allowed Return on Equity
Percent



Allowed returns in 2004 and 2005 decreased due to lower bond yields.

2004-2007 Performance Based Rate Plan

In July 2003, Terasen Gas received BCUC approval of a negotiated settlement for a 2004-2007 PBR. The PBR settlement establishes a process for determining Terasen Gas' delivery charges and incentive mechanisms for improved operating efficiencies. The four-year agreement includes incentives for Terasen Gas to operate more efficiently through the sharing of the benefits between Terasen Gas and its customers. The PBR Settlement includes 10 service quality measures designed to ensure Terasen Gas maintains service levels. It also sets out the requirements for an annual review process which will provide a forum for discussion between Terasen Gas and interested parties regarding its current performance and future activities.

Operation and maintenance costs and base capital expenditures are subject to an incentive formula reflecting increasing costs due to customer growth and inflation, less a productivity factor based on 50 percent of inflation during the first two years of the PBR and 66 percent of inflation during the last two years. Base capital expenditure amounts are a function of customer numbers and projected customer additions. The PBR Settlement provides for a 50/50 sharing mechanism of earnings above or below the allowed return on equity, beginning in 2004.

Upon expiry of the 2004-2007 PBR, there is no certainty as to whether a new negotiated settlement will be entered into, or what the terms of a new settlement might be.

Natural Gas Commodity Unbundling

Over the past several years, Terasen Gas, the BCUC, and interested parties have laid the groundwork for the introduction of natural gas commodity unbundling for commercial customers. On May 1, 2004, commercial customers of Terasen Gas became eligible to sign up to buy their natural gas commodity supply from third party suppliers beginning November 1, 2004. Terasen Gas will continue to provide delivery of the natural gas. Approximately 78,000 commercial customers are eligible to participate in commodity unbundling. By December 2004, 2,067 customers elected to participate in this program. The introduction of the unbundling program is not expected to have a material impact on the Company's financial results.

Regulation–TGVI

TGVI is also regulated by the BCUC. In 1995, an agreement was entered into between TGVI, the Province of British Columbia (the Province) and the Government of Canada, which included a Special Direction that was issued to the BCUC. The agreement, which expires no sooner than 2011, includes the following terms:

- TGVI receives, for the benefit of its customers, an annual payment until 2011 from the Province based on the wellhead price of natural gas in B.C. This payment amounted to $33.2 million in 2004.

- The accumulated revenue deficiency resulting from overall revenues being below the cost of service prior to 2003 had been recorded in a Revenue Deficiency Deferral Account (RDDA). When Terasen acquired TGVI, the amount of the RDDA was $85 million, for which Terasen paid a price of $61 million. The accumulated RDDA recorded on Terasen's consolidated financial statements totaled $45.6 million as at December 31, 2004, corresponding to a balance for TGVI regulatory purposes of $61.1 million, down $14.2 million from December 31, 2003. Terasen is committed to fund these revenue deficiencies by purchasing preferred shares or subordinated debt issued by TGVI. The BCUC was directed to set rates beginning in 2003 that amortize the RDDA balance over the shortest period reasonably possible, having regard for TGVI's competitive position relative to alternative energy sources and the desirability of reasonable rates.

- Any variances in the achieved ROE in a particular year from the allowed ROE (other than variances resulting from operation and maintenance costs) are deferred and recorded in the RDDA. The RDDA accumulated by TGVI is funded by the Company. Recovery of the deficiency through rates charged to customers is dependent upon regulatory approval and must be balanced against maintaining the competitiveness of TGVI's service relative to alternative energy sources. As a result, most risks associated with TGVI's annual financial results (other than operating costs) are, subject to BCUC approval, transferred to customers through the RDDA. The Company began recovery of the deficiency in 2003.

TGVI's three-year regulatory settlement took effect January 1, 2003. It provides for a continuation of the operation and maintenance cost incentive arrangements previously in place, and increases the allowed ROE for TGVI to a rate that is 0.50% higher than the allowed ROE for Terasen Gas, which equates to 9.53% for 2005. TGVI's allowed ROE in 2004 was 9.65%.

To ensure prompt recovery of the RDDA, the BCUC has approved a rate-setting mechanism for TGVI whereby customer rates are set at levels in excess of TGVI's cost of service, but below comparable electric rates. This has resulted in significant RDDA amortization in both 2003 and 2004.

Regulation–Trans Mountain

The National Energy Board (NEB) regulates the Canadian portion of Trans Mountain's crude oil and refined products pipeline system. The NEB authorizes pipeline construction and establishes tolls and conditions of service.

In November 2000, Trans Mountain and shipper representatives reached a negotiated agreement to determine Trans Mountain's tolls for the period 2001-2005. This ITS was approved by the NEB on March 22, 2001 to take effect as of January 1, 2001.

The 2001-2005 ITS establishes base tolls, within a band of approximately 179,000 to 201,000 bpd, on Trans Mountain's Canadian mainline for the term of the settlement. Base tolls are set using a throughput level of approximately 189,000 bpd. Any revenue shortfalls arising from annual throughput levels below 179,000 bpd are recovered from the shippers. Incremental revenues arising from annual throughput above 201,000 bpd are shared equally between Trans Mountain and the shippers. The base tolls do not escalate with inflation unless Canadian inflation rates increase above 3.5%. Trans Mountain keeps all of the benefits achieved through productivity initiatives and operating efficiencies.

Trans Mountain has initiated discussions with shipper representatives to extend or renew the 2001-2005 ITS. There is no certainty as to whether a new toll settlement will be entered into, or what the terms of a new toll settlement might be. Trans Mountain's earnings could be materially negatively impacted in 2006 depending on the final tolling arrangements with shippers.

The toll charged for the U.S. portion of Trans Mountain's pipeline in Washington State falls under the jurisdiction of the Federal Energy Regulatory Commission (FERC). Regulation by FERC is on a complaint basis. There were no complaints in 2004.

Regulation – Corridor

As an intra-provincial pipeline system, Corridor is subject to the jurisdiction of the Alberta Energy and Utilities Board (AEUB). With respect to Corridor, matters such as rates of return, construction and operation of facilities, and tolls are governed by contractual arrangements with shippers.

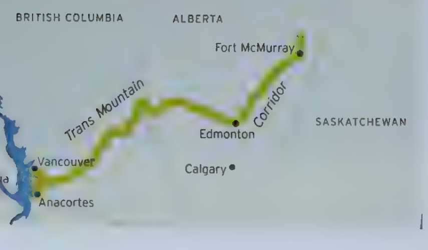
The Firm Service Agreement (FSA) between Corridor and its shippers sets pipeline tolls based on conventional cost of service mechanisms. The FSA is a 25-year agreement, with return on equity linked to prevailing long Canada bond yields. Shell Canada Limited, Chevron Canada Limited and Western Oil Sands L.P. have entered into a long-term ship-or-pay contract with Corridor for 60%, 20% and 20%, respectively, of the available capacity on the Corridor Pipeline.

Regulation – Express System

The Canadian segment of the Express Pipeline is regulated by the NEB as a Group 2 pipeline, which results in rates and terms of service being regulated on a complaint basis only. The U.S. segment of the Express Pipeline and the Platte Pipeline are regulated by the FERC, which regulates the rates and terms of service of a common carrier. FERC has additionally established methods by which pipelines may increase their rates.

Express committed rates are subject to a 2% inflator adjustment on April 1 of each year. Uncommitted or ceiling rates for both the U.S. segment of Express Pipeline and Platte Pipeline are subject to adjustment in accordance with FERC's annual indexation formula. Platte has historically been unable to charge its ceiling rates and has had to discount its rates because of market fundamentals in the Chicago/Wood River refining region. With changes in market conditions over the past year, Platte has been able to successfully remove and/or reduce many of its discounts. Today, Platte only has discounts from Casper and Guernsey to Wood River and from Casper to Guernsey; all other rates are at the applicable ceiling level.

Additionally, movements on the Platte Pipeline within the State of Wyoming are regulated by the Wyoming Public Service Commission (WPSC), which regulates the tariffs and terms of service of public utilities that operate in the State of Wyoming. The WPSC standards applicable to rates are similar to those of the FERC and the NEB.



In late 2003 and 2004, Terasen conducted open seasons to obtain long-term commitments for a portion of its current uncommitted capacity and for expansion capacity, the latter available in April 2005. The results of the open seasons were very positive and based upon current capacity of 172,000 bpd, Express has 85% committed through long-term contracts. Post-expansion, Express will have 84% of the 280,000 bpd total capacity contracted. These contracts expire in 2007, 2012, 2014 and 2015 in amounts of 1%, 40%, 11% and 32% of total capacity, respectively. These contracts provide for committed tolls for transportation on the Express System, which can be increased each year by up to 2%. The remaining capacity is made available to shippers as uncommitted capacity and was fully utilized in 2004.

RISK MANAGEMENT AND GOVERNANCE

In order to ensure that operating and financial results meet customer, regulatory and shareholder expectations, an effective system of risk management and governance is essential. Terasen has an Enterprise Risk Management (ERM) framework, methodology, and risk management process across the organization to ensure that significant business risks are identified, evaluated and appropriately managed and monitored. Terasen's corporate governance practices are described more fully in Terasen's management proxy circular in connection with the 2004 annual shareholders' meeting.

Pursuant to Multilateral Instrument 52-109 – Certification of Disclosure in Issuers' Annual and Interim Filings (MI52-109), Terasen's management is actively evaluating the effectiveness of the design and operation of the Company's disclosure controls and procedures in consultation with external consultants. The evaluation is being conducted under the supervision of, and with the participation of, the President and Chief Executive Officer and the Senior Vice President, Finance and Chief Financial Officer.

Terasen takes its responsibilities under MI52-109 very seriously. Terasen is leveraging the existing ERM framework, methodology, and risk management process to apply a consistent risk-based approach to certification compliance efforts. Terasen's rigorous risk management and reporting mechanisms, together with tight linkage between risk management and the annual enterprise-wide internal audit plan, are factors that reduce the enterprise's risk with regards to potential misrepresentations, misstatements and internal control weaknesses.

ASSET MANAGEMENT

The focus of asset management is to ensure reliable, cost effective, quality service with full regard for the safety of employees and the public while operating in an environmentally responsible manner. Appropriate regulatory arrangements provide incentives to manage costs and maintain or improve service quality. Once opportunities are available, asset management skills are key to capitalizing on these incentives.

At the core of Terasen's businesses is the ability to safely, reliably and efficiently provide energy transportation and utility infrastructure management services. In the provision of these services, the Company has implemented an operating and risk management framework to enable it to consistently achieve its financial and operating targets. In addition, the framework has enabled Terasen to leverage its operating expertise to additional utility businesses, providing further opportunities for value creation.

The natural gas distribution and petroleum transportation businesses maintain comprehensive facility risk assessment, pipeline integrity management and damage prevention programs, and pipeline security systems as preventive measures to mitigate the risk of a pipeline failure or other loss of system integrity. These programs are intended to reduce both the likelihood and severity of the business interruption and/or environmental liability that could result from a pipeline failure or loss of integrity.

The actions necessary to abandon pipeline systems at the eventual end of their useful lives have not been defined and the costs of these actions are not currently determinable and may not be fully recovered in rates or tolls. Until such time as the specified requirements of abandonment and the funding mechanism for the eventual recovery of negative salvage is determined, the Company's petroleum transportation and gas distribution businesses, like those of other Canadian pipeline systems, make no provision for these amounts.

Terasen's operating subsidiaries could be exposed to significant operational disruptions and environmental liability in the event of a petroleum product spill or an accident involving natural gas or a compromise to water or sewer distribution systems operated and/or maintained by the Company. Terasen has taken all reasonable and prudent steps to minimize its exposure in the case of a catastrophic event or environmental upset. The Company conducts its operations under the direction of an Environmental Management System which specifies impacts, control measures and audit protocols. The Company also has an insurance program that provides coverage for liability and property damage.

Terasen has detailed emergency preparedness plans in place to respond to natural disasters, accidents and emergencies, and regularly tests these plans in simulations involving employees and other emergency response organizations. The Company is also committed to monitor and assess its safety and environmental performance regularly. Terasen incorporates safety performance measures into its employee compensation system, sets targets and objectives for environmental performance, and conducts safety and environmental audits.

Safety and environmental management is a key aspect of effective asset management. Terasen Gas has established programs to use resources more efficiently and effectively including a greenhouse gas management program, industrial waste recycling and salvage shop operations. For the sixth consecutive year, Terasen Gas was awarded gold level reporting status from Canada's Climate Change Voluntary Challenge and Registry (VCR). In 2003, Terasen Gas received the VCR Leadership award, becoming the only company in its sector to receive the honour twice, having previously received the award in 2001. The VCR ranking acknowledges Terasen Gas' efforts to develop specific measures and voluntarily set reduction targets. In 2003 Terasen Gas reduced its operating emissions 5% below 2000 levels (before offsets) and 14% below 2000 levels, after accounting for offset project emission reductions. These results were accomplished through operational efficiencies, equipment selection and offset project investment.

Through the terms of its regulatory settlements, Terasen Gas has been successful in achieving and exceeding its productivity targets and capitalizing on incentives. A recent independent analysis of operating costs found that Terasen Gas was the best performer among ten Canadian gas distribution utilities on the measures of customers per employee and operating costs per customer.

Terasen's petroleum transportation business has also taken steps to improve operating cost efficiency under Trans Mountain's Incentive Toll Settlement.

BUSINESS AND PROJECT DEVELOPMENT

Terasen's success in business and project development is expected to come through a combination of greenfield expansions of existing assets and accretive acquisitions of complementary assets. The Company is working closely with its customers in each area of its business to develop opportunities which create value for both the customers and its shareholders.

In 2004, Terasen continued to demonstrate its project management skills through the on-time completion of the Trans Mountain pipeline capacity upgrade, which added 27,000 bpd of throughput. The risks associated with construction projects require that the Company maintains strong project management capabilities. The construction of the Southern Crossing and Corridor pipelines on-time and on-budget, along with existing pipeline expansions, has demonstrated Terasen's project management and execution skills, which will continue to be applied to new infrastructure construction opportunities. A key aspect of construction project management for Terasen is ensuring that contractors are responsible for risks that they can best manage.

Through the acquisition of TGVI, the Express System, and several water and utility service providers, Terasen has demonstrated its ability to successfully integrate acquisitions and achieve operating efficiencies. In the end, the ability to successfully integrate new acquisitions will have a significant impact on the Company's ability to achieve value-accretive acquisitions.

Terasen actively pursues development and acquisition opportunities in North America, where these opportunities are in related businesses, are compatible with Terasen's operating competencies, are located in a manageable region, and above all provide a positive financial impact. The entry into new markets and non-regulated businesses may require the Company to undertake additional risk, such as currency risk or regulatory risk. In order to proceed with projects that may expose Terasen to additional risk, the Company requires above-normal returns from the project and active risk management and other mitigating strategies are employed.

ENERGY MARKET CONDITIONS

Terasen's financial performance, business development success, and acquisition opportunities are impacted by energy market conditions including, but not limited to, general economic conditions, market competitiveness, changes in demand and supply, and commodity prices. The Company has in place various risk management activities designed to mitigate the impact of these factors on its operating and financial performance. The following is a discussion of the key energy market conditions that affect Terasen's business and the activities designed to manage the Company's exposure to market risk.

Competitiveness – Natural gas maintains a competitive advantage in terms of pricing when compared with alternative sources of energy in British Columbia. However, because electricity prices in British Columbia continue to be set based on the historical average cost of production (primarily hydro-electric dams), rather than based on market forces, they have remained artificially low compared to market priced electricity and, as a result, marginally higher than market-based natural gas costs. Over time, these pricing signals may distort energy use decisions by British Columbia consumers, thereby decreasing the use of natural gas by customers. Terasen Gas and TGVI are working with BC Hydro on demand side management and partnering with communities to assess how the Company can best serve them in the future.

Trans Mountain's pipeline to the West Coast of North America and the Express System to the U.S. Rocky Mountains and Midwest are two of several pipeline alternatives for Western Canadian petroleum production, and throughput on these pipelines may decline if overall petroleum production in Alberta declines or if tolls become uncompetitive compared to alternatives. The Company's oil transportation business competes against other pipeline companies who could be in a position to offer different

tolling structures, which may provide a competitive advantage in new pipeline development. Throughput on Trans Mountain may decline in situations where West Coast petroleum prices, net of transportation costs, are relatively lower than alternative prices in the U.S. Midwest. Throughput on the Express System may decline as a result of reduced petroleum product demand in the U.S. Rocky Mountains.

Impact of Changes in Economic Conditions – New customer additions at Terasen Gas and TGVI are typically a result of population growth and new housing starts, which are affected by the state of the provincial economy. The Company is also affected by changes in trends in housing starts from single-family dwellings to multi-family dwellings, for which natural gas has a lower penetration rate. While new housing starts have increased in B.C. in 2004, growth of new multi-family housing starts has significantly outpaced that of new single-family housing starts.

Fluctuations in natural gas use per residential and commercial customer, whether arising from weather or price levels, are deferred and recovered in customer rates and have no earnings impact on the Company.

Throughput on Terasen's petroleum pipelines and future business development is dependent on the supply of, and demand for, crude oil and other liquid hydrocarbons, particularly from the Alberta oilsands. Changes in the business environment, such as a decline in crude oil prices, an increase in production costs from higher feedstock prices, supply disruptions, or higher development costs, could result in a slowing of supply from the Alberta oilsands. In addition, changes in the regulatory environment or governmental policies, such as the Kyoto Protocol, may have an impact on the supply of crude oil.

Throughput on Terasen's petroleum pipelines may decline as a result of changes in business conditions. However, under the ITS for the Trans Mountain Canadian mainline, this risk is mitigated by a mechanism that permits Trans Mountain to recover revenue shortfalls arising from average throughput below 179,000 bpd through toll adjustments in subsequent years. Declines in Express revenues are mitigated by shipper firm service contracts as noted in the section "Regulation – Express System". Throughput on the Corridor pipeline is backed by long-term take-or-pay contracts with the shippers.

Commodity Prices – The Company employs a number of tools to reduce its exposure to natural gas price volatility. These include purchasing gas for storage and adopting hedging strategies, which include a combination of both physical and financial transactions, to reduce price volatility and ensure natural gas commodity costs remain competitive against electric rates. Activities related to the hedging of gas prices are approved by the BCUC and gains or losses accrue entirely to customers. The Company's commodity derivatives are discussed more fully in the section "Financial Instruments".

Deregulation of the electric industry, particularly in Alberta and Montana, has increased Terasen's price risk associated with the operation of the Trans Mountain and Express pipeline systems. Terasen has developed a two-year power purchasing plan to mitigate the risk associated with fluctuations in power prices, and a power management system is being used to more effectively predict power usage.

Natural Gas Supply – By bringing the Southern Crossing Pipeline into service in 2000, Terasen Gas has improved the security and competitiveness of the gas supply arrangements in place for Terasen Gas' customers. To the extent possible, Terasen Gas and TGVI have also minimized gas supply and price risk through the use of long-term transportation, storage and supply contracts, hedging instruments, and a diverse supply portfolio.

However, regional market prices have been higher from time to time than prices elsewhere in North America as a result of insufficient peak pipeline capacity to serve the increasing demand for natural gas in B.C. and the U.S. Pacific Northwest. In addition, Terasen Gas and TGVI continue to be dependent on a limited selection of pipeline and storage providers, particularly in the Vancouver, Fraser Valley and Vancouver Island service areas where the majority of the Company's natural gas distribution customers are located. Terasen is actively exploring opportunities to cost-effectively expand pipeline capacity to the Lower Mainland through initiatives such as the Inland Pacific Connector Project–a proposal to extend the Southern Crossing Pipeline from Oliver (in the interior of British Columbia) to the regional natural gas trading hub of Sumas, near Vancouver.

Terasen Gas and TGVI are critically dependent on a single source transmission pipeline. Terasen Gas is reducing its dependency on the Duke transmission system by increasing its scale and diversification of gas supply through the development of the Southern Crossing Pipeline and proposed Inland Pacific Connector. In the event of a service disruption on the transmission system, the Vancouver Island portion of the system could be affected for an extended period of time, thereby affecting revenues. Proceeding with the proposed liquefied natural gas (LNG) storage facility on Vancouver Island would serve to reduce this exposure. Terasen Gas is also supporting TGVI in its efforts to provide additional gas transportation capacity on Vancouver Island. A more detailed discussion of TGVI's expansion plans is outlined in the section "Business Development". Terasen Gas has indicated to the BCUC, its willingness to lease storage capacity on the system if TGVI proceeds with the expansion.

ACCESS TO CAPITAL

In order to meet the capital investment and return requirements of its businesses, Terasen must have reliable access to cost effective capital. The Company's requirements for capital and access to capital are discussed more fully under "Liquidity and Capital Resources".

The development of income-oriented investment vehicles, such as income trusts, has lowered the cost of capital for certain companies and increased the prices that can be paid for acquisitions of certain infrastructure assets. In some circumstances, a corporate financing structure such as Terasen's stand-alone structure is unable to achieve a cost of capital that is as low as these alternative structures. In order to remain competitive in the pursuit of certain acquisitions, it may be necessary for Terasen to develop alternative structures that deliver a lower cost of capital or make the size of the transaction more reasonable from a risk management perspective.

An example of such an alternative structure is the consortium formed by Terasen to acquire the Express System. Terasen and two major Canadian pension funds each own a one-third interest in the Express System. The structure developed by Terasen results in a pairing of the pension funds' financial capabilities with Terasen's operating capabilities, while delivering attractive overall returns to Terasen on its investment.

Earnings and cash flow volatility arise from general financial market risk, including movements in interest rates and fluctuations in the Canadian dollar relative to other foreign currencies. Terasen has established risk management policies to oversee the use of derivative financial instruments designed to offset its exposure to financial market risk. Continuous monitoring and regular reporting to senior management are in place to assess the derivative activity. The Company does not use derivative financial instruments to engage in speculative transactions. The financial instruments outstanding are described in the section "Financial Instruments".

Interest Rates – Terasen's earnings are sensitive to interest rates in several ways. Some outstanding debt has exposure to short-term interest rates, and is not subject to regulatory interest deferral accounts. In addition, the allowed returns on equity for Terasen Gas, TGVI and Corridor are determined by formulae that result in lower allowed ROEs if long-term Canada bond yields decline. As a result, if short-term interest rates increased by 1.0% for an extended period of time, the estimated impact on Terasen's annual consolidated net earnings would be a reduction of approximately $3.1 million, whereas a similar decrease in long-term interest rates would be expected to decrease annual net earnings by approximately $10.9 million. Terasen has hedging programs in place for its interest rate and foreign exchange risks which have been factored into the sensitivities described above, and which are described in note 16 to the consolidated financial statements.

Foreign Exchange – In addition, a component of Terasen's earnings, principally earnings from Trans Mountain's U.S. pipeline, the Express System and U.S.-based water and utility services operations, are denominated in U.S. dollars. As a result, an annual decline of $0.10 in the price of a U.S. dollar in Canadian dollars would be expected to result in a decrease in annual consolidated net earnings of approximately Cdn$1.1 million.

Counterparty Credit Risk – The Company is exposed to credit risk in the event of non-performance by counterparties to derivative instruments. The Company is also exposed to significant credit risk on physical off-system natural gas sales. Because it deals with high credit quality institutions in accordance with established credit approval practices, the Company does not expect any counterparties to fail to meet their obligations.

The sensitivities described above are based on Terasen's business profile as at December 31, 2004 and may change over time as a result of changes in Terasen's business profile.

FINANCIAL AND CAPITAL MANAGEMENT

LIQUIDITY AND CAPITAL RESOURCES

Consolidated Cash Flow

Cash from operations refers to cash generated before the impact of working capital and deferral accounts. In 2004, Terasen generated $296.3 million in cash from operations, up $7.0 million from the year prior. The increase in cash from operations was primarily attributable to higher earnings for the year as adjusted for non-cash charges such as depreciation and amortization. Cash from operations was reduced by $14.3 million in 2004 as earnings from the Express System exceeded distributions, which were reinvested. Cash flow from operating activities, which includes the impact of changes in working capital and deferral accounts, increased to $342.0 million in 2004 from $269.8 million in 2003. In addition to higher earnings, cash flow from operating activities increased as a result of an increase in non-cash working capital balances in 2003, which were attributable to construction during 2002.

Terasen's working capital requirements fluctuate seasonally based on natural gas consumption. Given the low-risk, regulated nature of its business, Terasen is able to maintain negative working capital balances. Terasen maintains adequate committed credit facilities to meet its working capital requirements. On an annual basis, Terasen generates sufficient cash flow to meet its working capital requirements.

Terasen Inc. Consolidated Capital Expenditures
$ Millions

Capital expenditures are expected to increase in 2005 to support a variety of projects.

Capital Expenditures

Capital expenditures totaled $154.4 million in 2004 compared with $222.9 million in 2003. The primary reason for the decline in capital spending was the construction of the Corridor pipeline project, which was completed in 2003. The major capital expenditure in 2004 was the expansion of the Trans Mountain pipeline. In addition, Terasen acquired a 50% share of FSW and other smaller water and utility service companies for $57.9 million, which is not included in the table below. Actual capital spending in 2004 and forecast capital spending in 2005 is summarized as follows:

Capital Expenditures

In millions of dollars	**2004 Actual**	2005 Forecast
Natural gas distribution		
Terasen Gas	**$ 93.9**	$ 170.0
TGVI	**18.4**	70.0
	112.3	240.0
Petroleum transportation		
Trans Mountain	**28.0**	40.0
Terasen Pipelines Inc.	**2.6**	–
Corridor	**0.4**	10.0
	31.0	50.0
Water and utility services	**7.8**	50.0
Other	**3.3**	10.0
Total	**$ 154.4**	$ 350.0

Projected Capital Expenditures

Terasen has estimated total 2005 consolidated capital expenditures of $350 million. Major capital expenditures in 2005 for Terasen Gas and TGVI include the acquisition of the Coastal Facilities buildings ($50 million), the Fraser river crossing ($20 million), the purchase and upgrade of the Texada Island compressor station ($15 million) and initial expenditures on the construction of a liquefied natural gas storage facility on Vancouver Island ($23 million). Major project expenditures for pipeline transportation include the further development of the TMX project ($13.5 million) and the Corridor pipeline de-bottlenecking ($6.5 million). Water and utility services capital requirements in 2005 are primarily focused on greenfield development opportunities and minor acquisitions. The Company expects to finance capital expenditures with a combination of long-term debt, short-term borrowings and internally generated funds.

In April 2005, the US$100 million expansion of the Express System is expected to be completed. During July 2004, the Express partnership completed a long-term debt issue of US$110 million to finance the expansion. These expenditures are not included in the estimates above as Express is accounted for using the equity method.

Coverage Ratios

Due to the capital intensive nature of the Company's businesses and the need to raise debt frequently in the fixed income market, maintenance of its financial ratios is a priority for Terasen. The most significant ratios are considered to be interest coverage and equity as a percentage of total capital.

Financial Ratios	2004	2003
Interest coverage	**2.4**	2.1
Equity to total capital (as at December 31)	**35%**	33%
Common equity to total capital (as at December 31)	**32%**	30%

Interest coverage for Terasen improved in 2004 compared to 2003 mainly as a result of higher earnings and lower interest rates. Interest coverage is targeted to be at or above 2.0.

Equity to total capital includes the Capital Securities, which will be reclassified as a liability effective January 1, 2005. Prospectively, Terasen will target a common equity component of total capital (excluding capital securities) of between 30% and 33%. The Company does not anticipate any material changes in the relative mix or cost of its capital resources.

Terasen Inc. Equity to Total Capital
Percent

Terasen's financial strength has increased significantly.

Public Issues

In September 2003, Terasen Gas issued $150 million of medium term note debentures at a floating interest rate. In April 2004, Terasen Gas issued $150 million of 30-year medium term note debentures at an interest rate of 6.50%. In September 2004, Terasen Inc. issued $125 million of 10-year medium term note debentures at an interest rate of 5.56%.

In February 2005, Corridor issued $150 million each of 5-year and 10-year unsecured debentures at rates of 4.24% and 5.033%, respectively. Proceeds were used to repay commercial paper issued by Corridor. Funds generated from the issuance of medium term note debentures were used for general corporate purposes.

Lines of Credit

As at December 31, 2004, the Company had lines of credit in place totaling $1,527 million to finance cash requirements, comprising $300 million at Terasen, $500 million at Terasen Gas, $215 million at TGVI, and $512 million at Corridor. These lines enable the respective companies to borrow directly from their bankers, issue bankers' acceptances and support commercial paper issuance. Bank lines of $540 million were unutilized at the end of 2004. Virtually all short-term cash needs are funded through commercial paper and bankers' acceptances in the Canadian market at rates generally below bank prime. Terasen does not have, nor does it expect to have, any defaults or arrears.

Dividends

Dividends and distributions on common shares and capital securities totaled $93.0 million in 2004, compared to $86.1 million in 2003. The increase reflects an increase in the dividends paid on common shares in 2004.

Terasen Inc. Dividends Paid Per Share
Dollars

Dividends have increased consistently alongside earnings growth.

Restrictions on Dividends

Terasen Gas is not legally restricted from transferring funds to Terasen Inc., but is expected to maintain equity components similar to its respective deemed equity. Dividends that reduce equity below deemed levels could have adverse regulatory consequences. TGVI has restrictions on its ability to issue dividends within its credit agreements. Corridor's credit agreement restricts its ability to issue dividends subject to certain debt-to-total capital requirements. Cash distributions from Express are subject to limitations in the Express financing agreements and decisions made by the Express Board of Directors, which Terasen does not control. In 2004, none of these restrictions constrained the distribution of subsidiary earnings not otherwise needed for reinvestment.

Credit Ratings

Securities issued by Terasen, Terasen Gas, Trans Mountain and Corridor are rated by DBRS Inc. (DBRS) and Moody's Investors Service Inc. (Moody's). The ratings assigned to securities issued by the Terasen group of companies are reviewed by these agencies on an ongoing basis.

The table below summarizes the ratings assigned to the Company's various securities at December 31, 2004.

Credit Ratings	DBRS	Moody's
Terasen Inc.		
Commercial paper	R-1 (Low)	
Unsecured long-term debt	A (Low)	A3
Capital securities	BBB (High)	Baa1
Terasen Gas Inc.		
Commercial paper	R-1 (Low)	
Secured long-term debt	A	A1
Unsecured long-term debt	A	A2
Terasen Pipelines (Trans Mountain) Inc.		
Commercial paper	R-1 (Low)	
Unsecured long-term debt	A (Low)	
Terasen Pipelines (Corridor) Inc.		
Commercial paper	R-1 (Low)	
Unsecured long-term debt	A	A2

After reassessing its relationship with Standard & Poor's Ratings Services, a division of the McGraw-Hill Companies (Canada) Corporation (S&P), Terasen decided early in 2004 to discontinue the engagement of S&P to provide credit ratings on the debt of Terasen and Terasen Gas. Terasen believes the credit ratings issued by Moody's and DBRS will be sufficient to service the requirements of creditors and maintain the Company's access to capital. S&P continues to provide an unsolicited rating on Terasen's outstanding debt based on publicly available information. As of December 31, 2004, Terasen's unsecured long-term debt was rated BBB- by S&P.

There is a provision in Terasen's $300 million credit facilities that a downgrade below BBB (low) or Baa3 by DBRS or Moody's, respectively, would shorten the remaining term of Terasen's credit facility to ten months.

Contractual Obligations

The table below sets forth Terasen's financial obligations due in the years indicated.

In millions of dollars	Total	2005	2006-2007	2008-2010	2011 and later
Long-term debt	$ 2,572.5	$ 414.5	$ 932.5	$ 517.1	$ 708.4
Capital lease obligations	10.8	2.2	4.4	4.2	–
Operating leases	252.8	24.1	44.3	59.9	124.5
Purchase obligations[1]	1,197.9	766.8	395.1	36.0	–
Other long-term obligations	44.5	1.2	2.7	4.8	35.8
Total contractual obligations	$ 4,078.5	$ 1,208.8	$ 1,379.0	$ 622.0	$ 868.7

[1]Purchase obligations includes gas purchase contracts that are based on market prices that vary with gas commodity indices. The amounts disclosed reflect index prices that were in effect at December 31, 2004.

Gas purchase agreements contain provisions whereby Terasen Gas and TGVI could be obliged to provide security to gas suppliers if they have reasonable grounds. Terasen has arranged committed credit facilities that the Company believes would be adequate to meet these requirements.

Off-Balance Sheet Arrangements

In 2000, Terasen Gas entered into a leasing arrangement with a syndicate of Canadian banks and the BCG Coastal Facilities Trust, a special-purpose entity, to finance new building facilities in the Greater Vancouver area. The Coastal Facilities synthetic lease agreement had been accounted for as an off-balance sheet item. As at December 31, 2004, the value of the Coastal Facilities leasing agreement was approximately $49.4 million. Lease payments of approximately $4.5 million were made by Terasen Gas in 2004.

In 2004, Terasen Gas applied to the BCUC for and received approval to unwind the synthetic lease and include the Coastal Facilities assets in rate base. On January 4, 2005, Terasen Gas paid approximately $49.4 million to BCG Coastal Facilities Trust to unwind the synthetic lease. Accordingly, payments related to this operating lease are not included in the above table. The Coastal Facilities assets have been included in the Terasen Gas rate base commencing January 2005.

Other than the Coastal Facilities lease, which has been refinanced, there are no other material off-balance sheet agreements.

FINANCIAL INSTRUMENTS

Fair Value Estimates

The fair value of the Company's long-term debt, calculated by discounting the future cash flow of each debt issue at the estimated yield to maturity for the same or similar issues at December 31, 2004, or by using available quoted market prices, is estimated at $2,818.2 million. The majority of the Company's long-term debt relates to regulated operations which enables the Company to recover the existing financing charges through rates or tolls.

Fair value estimates are made at a specific point in time, based on relevant market information and information about the financial instrument. These estimates cannot be determined with precision as they are subjective in nature and involve uncertainties and matters of judgment.

Derivative Instruments

The Company uses derivative instruments to hedge its exposures to fluctuations in natural gas prices, interest rates and foreign currency exchange rates. As approved by the regulator, derivatives are used to manage natural gas price risk in the natural gas distribution operations. The majority of the natural gas supply contracts have floating rather than fixed prices. The Company uses natural gas price swap contracts to fix the effective purchase price. Any differences between the effective cost of natural gas purchased and the price of natural gas included in rates are recorded in a deferral account (MCRA and CCRA) and, subject to regulatory approval, are passed through in future rates to customers.

The Company's short-term borrowings and variable rate long-term debt are exposed to interest rate risk. The Company manages interest rate risk through the use of interest rate derivatives. Foreign currency risk in natural gas distribution operations relates mainly to purchases and sales of natural gas denominated in U.S. dollars, and is thereby managed through regulatory deferral accounts. Certain foreign currency risks in the natural gas distribution operations are managed through the use of foreign currency derivatives on behalf of customers.

The Company's earnings from the U.S. portion of Trans Mountain's crude oil pipeline system and the Company's investment in the Express System are subject to foreign currency risk. The Company's earnings are also subject to translation risk associated with certain Express System assets and liabilities. The Company manages these foreign currency exposures through the use of foreign currency derivatives.

Asset (Liability) *in millions*	Number of swaps	Term to maturity	**December 31, 2004** Carrying Value	**December 31, 2004** Fair Value	December 31, 2003 Carrying Value	December 31, 2003 Fair Value
Interest Rate Swaps						
Terasen Inc.[1]	2	05/06–12/08	**$ 0.4**	**$ 5.4**	$ 0.4	$ 5.3
TGVI[1]	4	05/06–12/08	**(0.5)**	**(3.2)**	(1.5)	(4.8)
Natural Gas Commodity Swaps						
Terasen Gas and TGVI[2]	139	02/05–10/06	**1.9**	**(8.3)**	(7.8)	6.3
Clean Energy[3]	7	01/05–12/09	**6.5**	**6.5**	—	—
Foreign Currency Swaps						
Terasen Inc.[4]	2	01/05	**(0.6)**	**(0.6)**	0.8	0.8
Terasen Gas	—	—	—	—	—	(0.9)

[1]The interest rate derivatives entered into by Terasen Inc. resulted in a $3.6 million contribution to earnings in 2004, compared with a $2.2 million contribution in 2003. The derivatives entered into by TGVI relate to regulated operations and any resulting gains or losses are recorded in a deferral account (RDDA), subject to regulatory approval, and passed through to customers in future rates.

[2]The natural gas derivatives fair value reflects only the value of the natural gas derivatives and not the offsetting change in value of the underlying future purchases of natural gas. These fair values reflect the estimated amounts the Company would receive or pay to terminate the contracts at the stated dates.

[3]Clean Energy enters into natural gas commodity derivatives to manage its exposure to the cost of natural gas. Effective January 1, 2004, gains and losses on these transactions are recognized in income in accordance with the Company's adoption of the new accounting guideline on hedging relationships. During the twelve months ended December 31, 2004, $6.5 million of gross unrealized pre-tax gains were recognized in income. The carrying and fair value of Clean Energy's natural gas commodity swap represents Terasen's 45.0% ownership interest.

[4]The change in fair value of the derivatives of $0.7 million has been included in the earnings contribution from the Express System for the twelve months ended December 31, 2004.

OUTSTANDING SHARE DATA

December 31, 2004

Common shares issued and outstanding	114,355,665
Less: Common shares held by Terasen Pipelines (Trans Mountain) Inc.	9,184,188
	105,171,477
8.0% capital securities issued and outstanding	$ 125,000,000
Options outstanding	2,905,487
Options exercisable	1,369,365

The 8.0% capital securities are exchangeable on or after April 19, 2010 for common shares of the Company at 90% of the market price, subject to the right of the Company to redeem the securities for cash. A maximum of 125,000,000 common shares could be issued if this right was exercised.

FINANCIAL RESULTS

EARNINGS PERFORMANCE

In 2004, Terasen reported earnings of $149.8 million, an increase of $17.1 million over earnings of $132.7 million in 2003. On a per share basis, earnings increased to $1.43 per share in 2004, compared with $1.28 per share in 2003. Included in 2004 earnings was a $3.3 million gain arising from Clean Energy's price risk management activities. Clean Energy makes use of natural gas derivatives as part of its price risk management strategy and is exposed to quarterly mark-to-market valuations. Excluding the gain, Terasen's earnings were $146.5 million, or $1.40 per share, up 6.9% over 2003 earnings per share before non-recurring items of $1.31.

During the year, dividends paid per common share were $0.825, up 7.8% from $0.765 per share in 2003. In April 2004, Terasen's Board of Directors approved a two-for-one stock split of the Company's common shares outstanding. All per share amounts have been restated to reflect the two-for-one stock split, which took effect in June 2004.

In the fourth quarter of 2004, net earnings were $53.9 million, or $0.51 per share, compared with earnings of $50.9 million, or $0.49 per share in the fourth quarter of 2003. The increase in earnings in the fourth quarter was driven mainly by an increase in earnings contribution from Trans Mountain and Express. Terasen recorded a $3.4 million restructuring charge in the fourth quarter of 2003, associated with the operational integration of Terasen Gas and TGVI.

Earnings applicable to common shares were $149.8 million in 2004 compared to $132.7 million in 2003. An analysis of the increase in earnings is as follows:

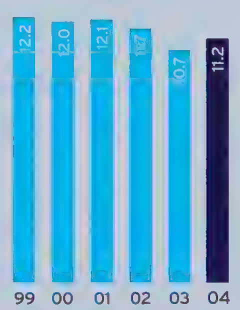
In millions of dollars

Earnings applicable to common shares for 2003	$ 132.7
Non-recurring items in 2003[1]	3.4
Earnings before non-recurring items in 2003	136.1
Natural Gas Distribution	
Reduction in allowed ROE	(2.4)
Operational efficiencies	4.1
Introduction of earnings sharing mechanism	(4.7)
Other items	0.1
Petroleum Transportation	
Increase in earnings from the Express System (before foreign exchange loss)	2.6
Express foreign exchange loss in 2003	3.6
Increase in earnings from the Corridor pipeline (full year in 2004)	4.9
Higher throughput and other items	3.6
Water and Utility Services	
Organic growth in water and utility services business	1.3
Contributions from Fairbanks and other minor acquisitions	1.2
Other Activities	
Higher corporate expenses, financing costs, and other items	(3.9)
Gain on Clean Energy's price risk management activities	3.3
Earnings applicable to common shares for 2004	$ 149.8

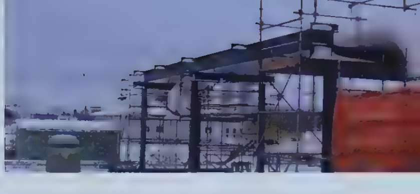
Terasen Inc.
Earnings Per Share
(Before Non-Recurring Items)
Dollars

Terasen has consistently delivered on its target of six per cent annual earnings per share growth.

Terasen Inc.
Return on Common Equity
(Before Non-Recurring Items)
Percent



Despite lower interest rates, the company has sustained attractive returns on equity.



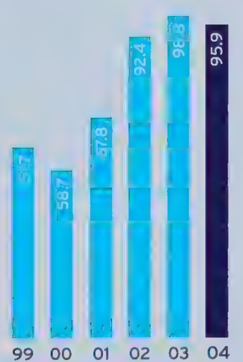
Earnings applicable to common shares were $132.7 million in 2003 compared to $105.8 million in 2002. An analysis of the increase in earnings is as follows:

In millions of dollars	
Earnings applicable to common shares for 2002	$ 105.8
Natural Gas Distribution	
Increase in RDDA discount accretion	2.5
Lower income tax rates and other items	3.9
Petroleum Transportation	
Earnings from the acquisition of the Express System (before foreign exchange loss)	13.3
Express foreign exchange loss	(3.6)
Earnings from the Corridor pipeline	10.7
Higher throughput and other items	6.5
Water and Utility Services	
Growth in water and utility services business	3.2
Other Activities	
Higher corporate expenses, financing costs, and other items	(8.5)
Lower write-down of investment in Westport Innovations Inc.	2.3
Earnings before non-recurring items in 2003	136.1
Non-recurring items[1]	(3.4)
Earnings applicable to common shares for 2003	$ 132.7

NON-GAAP MEASURES

[1]Terasen discloses earnings before non-recurring items in order to assist investors in evaluating which components of the Company's earnings are likely to be sustainable in future years. For this purpose, the Company identifies non-recurring items, which are material gains and losses that, in management's opinion, arise from events or circumstances that are not expected to occur on a regular basis. Earnings before non-recurring items do not have any standardized meaning prescribed by generally accepted accounting principles, and therefore may not be comparable to similar measures presented by other Canadian issuers of securities. In 2003, Terasen incurred a non-recurring restructuring charge of $3.4 million after-tax related to the integration of Terasen Gas and TGVI. There were no material non-recurring items in 2004.

Natural Gas Distribution Earnings
(Before Non-Recurring Items)
$ Millions



A lower allowed ROE in 2004 was offset by efficiency gains.

Natural Gas Distribution

In millions of dollars	**2004**	2003	2002
Revenues	**$ 1,494.1**	$ 1,497.9	$ 1,402.7
Operating expenses			
Cost of natural gas	**885.4**	889.7	807.2
Operation and maintenance	**190.5**	184.2	179.3
Depreciation and amortization	**98.7**	92.5	92.6
Property and other taxes	**47.1**	48.6	46.9
	1,221.7	1,215.0	1,126.0
Operating income	**272.4**	282.9	276.7
Financing costs	**126.2**	135.5	136.8
Earnings before income taxes	**146.2**	147.4	139.9
Income taxes	**50.3**	48.6	47.5
Earnings before non-recurring items	**95.9**	98.8	92.4
Non-recurring items	**—**	(3.4)	–
Earnings applicable to common shares	**$ 95.9**	$ 95.4	$ 92.4

Revenues from natural gas distribution declined to $1,494.1 million during 2004 from $1,497.9 million in 2003. Revenues are set at levels designed to recover the cost of delivery service of Terasen Gas and TGVI, together with the cost of the natural gas commodity. As a result, changes in consumption levels and changes in the commodity cost of natural gas do not materially impact revenue or earnings due to regulatory deferral accounts. The decline in revenue in 2004 was attributable to lower consumption, which more than offset the increase in the commodity cost recovered in rates charged to customers, which became effective in the third quarter of 2004.

Natural Gas Distribution Customer Additions

Customer additions grew as a result of strong housing starts in B.C.

Terasen Gas net customer additions during 2004 were 11,750, while TGVI's net number of customers increased by 4,233 in 2004. This brings the total number of utility customers to 875,166 at year-end. The total increase of 15,983 customers in 2004 was up from the 8,484 net customer additions recorded in 2003. Solid economic conditions and continued strength in new housing starts in British Columbia helped drive the net customer additions in 2004.

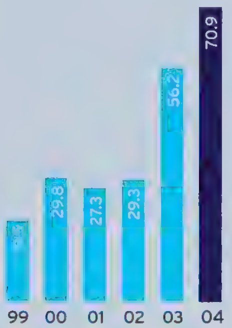
Terasen Gas industrial sales volumes decreased by 621 terajoules while transportation volumes increased by 511 terajoules from the previous year. Terasen Gas earns approximately the same margin regardless of whether a customer contracts for sales or transportation service. In 2004, the cost of natural gas declined to $885.4 million, from $889.7 million in 2003. Lower natural gas sales volume in 2004 more than offset the increase in the commodity cost of natural gas during the year.

Operating and maintenance expenses (excluding a $5.2 million pre-tax restructuring charge in 2003) increased to $190.5 million in 2004 from $184.2 million in 2003. The primary driver of higher operating expenses was an increase in insurance costs and transmission integrity costs, which are recoverable through customer rates. Depreciation and amortization increased by $6.2 million as a result of a higher rate base and an increase in the approved rate of depreciation and amortization.

Financing costs declined to $126.2 million in 2004 from $135.5 million in the previous year. The decline was mainly a result of lower short-term debt balances and lower interest rates.

Revenue from natural gas distribution declined to $495.7 million in the fourth quarter of 2004, down from $517.6 million in the same period of 2003. Revenue declined as a result of lower natural gas sales volumes due to warmer weather relative to the corresponding quarter of 2003. Earnings before non-recurring items from natural gas distribution declined to $42.6 million in the fourth quarter of 2004, from $44.8 million in the fourth quarter of 2003, mainly as a result of the lower allowed ROE. The natural gas distribution business recorded a $3.4 million restructuring charge in the fourth quarter of 2003.

Petroleum Transportation Earnings
(Before Non-Recurring Items)
$ Millions



Earnings have grown from $29.3 million in 2002 to $70.9 million in 2004 as a result of strong throughput, greenfield projects and acquisitions.

Trans Mountain Canadian Mainline Throughput
Barrels per day

Growth in Alberta oilsands production is contributing to strong pipeline throughput.

Petroleum Transportation

In millions of dollars	**2004**	2003	2002
Revenues	**$ 225.5**	$ 200.0	$ 136.0
Operating expenses			
Operation and maintenance	**66.0**	57.0	43.8
Depreciation and amortization	**35.9**	30.0	17.1
Property and other taxes	**22.5**	21.0	18.7
	124.4	108.0	79.6
Operating income	**101.1**	92.0	56.4
Financing costs	**22.5**	23.2	9.5
Earnings before contribution from Express	**78.6**	68.8	46.9
Contribution from Express	**15.0**	8.0	–
Earnings before income taxes	**93.6**	76.8	46.9
Income taxes	**22.7**	20.6	17.6
Earnings applicable to common shares	**$ 70.9**	$ 56.2	$ 29.3

Transportation Volumes

(bpd)	**2004**	2003	2002
Trans Mountain Canadian mainline	**236,100**	216,100	201,200
Trans Mountain U.S. mainline	**91,700**	54,600	47,800
Express System	**175,300**	171,200	167,000

Actual throughput on the Corridor Pipeline does not impact earnings as all of Corridor's capacity is contracted through ship-or-pay arrangements.

Revenues from petroleum transportation operations increased to $225.5 million in 2004 from $200.0 million in 2003. The increase was primarily a result of increased throughput on the Trans Mountain mainline and contributions from the Corridor Pipeline, which began commercial operations on May 1, 2003.

Average throughput on Trans Mountain's Canadian mainline increased to 236,100 bpd in 2004 from 216,100 bpd in 2003. Throughput on Trans Mountain remained solid throughout the year as there continued to be strong west coast demand for product from the Alberta oilsands. U.S. mainline deliveries averaged 91,700 bpd in 2004, compared to 54,600 bpd in 2003. Higher demand from Washington State and California refiners drove the increase in throughput on the U.S. mainline.

As discussed previously under Regulatory Arrangements, Trans Mountain's Canadian mainline is subject to a regulatory settlement that mitigates the impact on earnings of variations in throughput volumes outside a defined band. However, Trans Mountain's U.S. pipeline in Washington State is not subject to the same regulatory arrangements, and fluctuations in throughput on that pipeline will have a direct impact on petroleum transportation revenues and earnings. Fluctuations in throughput on the Express System will have a direct impact on Terasen's equity share of earnings, subject to the floor provided by the Express System's ship-or-pay contracts.

Operation and maintenance expenses increased to $66.0 million in 2004 from $57.0 million in 2003. Higher power costs, consistent with increased throughput, and Corridor's full-year of operations were the main drivers of increased operation and maintenance expense. Depreciation and amortization increased by $5.9 million to $35.9 million in 2004 as a result of the full-year contribution from the Corridor Pipeline.

Financing costs in 2004 were $22.5 million, compared with $23.2 million in 2003. The lower cost of financing was mainly due to lower interest rates.

The share of earnings from the Express System increased to $15.0 million in 2004 from $8.0 million in 2003. In 2003, the earnings contribution from Express included a $3.6 million foreign exchange loss. The increase in earnings contribution from Express in 2004 was a result of increased throughput, combined with earnings from reinvested cash distributions.

Revenue from petroleum transportation declined to $58.5 million in the fourth quarter of 2004, compared to $60.0 million in the fourth quarter of 2003. The decline in fourth quarter revenue was a result of lower tolls on Trans Mountain's Canadian mainline, which more than offset higher throughput during the period. Petroleum transportation reported earnings of $19.9 million in the fourth quarter of 2004, compared with $17.9 million in the fourth quarter of 2003. Higher earnings were driven by operating efficiencies at Trans Mountain and an increase in contributions from Express.

Water and Utility Services

In millions of dollars	**2004**	2003	2002
Revenues	**$ 201.6**	$ 152.5	$ 123.1
Operating expenses			
Cost of revenues	**152.4**	115.4	94.8
Operation and maintenance	**28.3**	21.4	22.7
Depreciation and amortization	**9.3**	8.0	4.1
Property and other taxes	**0.2**	0.1	0.2
	190.2	144.9	121.8
Operating income	**11.4**	7.6	1.3
Financing costs	**1.0**	0.9	–
Earnings before income taxes	**10.4**	6.7	1.3
Income taxes	**3.8**	2.6	0.4
Earnings applicable to common shares	**$ 6.6**	$ 4.1	$ 0.9

Water and utility services increased revenue by 32% in 2004 to $201.6 million from $152.5 million in 2003. The year-over-year increase in revenue was a result of growth in existing operations and the impact of the FSW acquisition and other minor acquisitions made in 2003 and 2004. Strong economic conditions in B.C. and Alberta helped to drive growth in the waterworks business.

In 2004, cost of revenues increased by 32% to $152.4 million, up from $115.4 million in 2003. Operation and maintenance expense in 2004 increased by 32% to $28.3 million, from $21.4 million in 2003. The increase in operation and maintenance expense and cost of revenues is consistent with the increase in revenues.

Depreciation and amortization increased in 2004, as compared with 2003, primarily as a result of the impact of acquisitions. Financing costs in 2004 remained essentially unchanged relative to 2003 as higher debt levels were offset by lower interest rates.

In the fourth quarter of 2004, revenue from water and utility services increased to $51.3 million from $32.9 million in the corresponding quarter of 2003. Operating income increased to $1.4 million for the three months ended December 31, 2004, compared with $1.3 million for the same period in 2003. Positive contributions from acquisitions

Water and Utility Services Earnings
(Before Non-Recurring Items)
$ Millions

Earnings in 2004 were $6.6 million, up 61% from 2003.

Results prior to 2002 are included in Other Activities.

combined with growth in existing operations drove the increase in operating income in the fourth quarter. The increase was partially offset by higher depreciation and business development costs in the fourth quarter of 2004, as compared with the fourth quarter of 2003. Overall, earnings contribution from the water and utility services business was $0.7 million in the fourth quarter of 2004, compared with $0.4 million in the corresponding quarter of 2003.

Other Activities

In millions of dollars	**2004**	2003	2002
Revenues	**$ 35.8**	$ 26.2	$ 45.4
Operating expenses			
Cost of revenues	**21.9**	17.0	25.4
Operation and maintenance	**18.1**	17.0	15.8
Depreciation and amortization	**3.2**	2.9	1.8
Property and other taxes	**0.3**	0.2	0.3
	43.5	37.1	43.3
Operating income (loss)	**(7.7)**	(10.9)	2.1
Financing costs	**16.9**	16.4	14.5
Loss before income taxes	**(24.6)**	(27.3)	(12.4)
Income tax (recovery)	**(7.6)**	(11.0)	(2.3)
Net loss	**(17.0)**	(16.3)	(10.1)
Capital securities distributions, net of income taxes	**6.6**	6.7	6.7
Loss applicable to common shares	**$ (23.6)**	$ (23.0)	$ (16.8)

Revenues from other activities increased to $35.8 million in 2004 from $26.2 million in 2003. Higher revenues were a result of improved operations in Terasen's International business and Clean Energy. Terasen intends to exit its International consulting business after the completion of existing contracts and commitments.

The operating loss from other activities improved to $7.7 million in 2004 from a loss of $10.9 million in 2003, which was primarily attributable to a $3.3 million after-tax gain from Clean Energy's price risk management activities. The gain was associated with Terasen's share of the increase of the fair values of Clean Energy's outstanding natural gas positions. Clean Energy makes use of natural gas derivatives as part of its price risk management strategy and is exposed to quarterly mark-to-market valuations.

Financing costs in 2004 were relatively unchanged from 2003 as higher outstanding debt balances were offset by lower interest rates.

In the fourth quarter of 2004, losses from other activities were $9.3 million, up from $8.8 million in the same quarter of 2003. The higher operating loss was due to an increase in financing costs and a lower tax recovery, as compared with the fourth quarter of 2003.

Other Activities Earnings (Loss)
(Before Non-Recurring Items)
$ Millions

Other activities include Clean Energy, Terasen International and corporate administration and financing costs.

Annual Financial Information

(dollars in millions except per share amounts)	2004	Year Ended December 31 2003	2002
Revenues	**$ 1,957.0**	$ 1,876.6	$ 1,707.2
Net earnings	**156.4**	139.4	112.5
Earnings applicable to common shares	**149.8**	132.7	105.8
Per common share–basic[1]	**1.43**	1.28	1.22
Per common share–fully diluted[1]	**1.42**	1.27	1.21
Dividends per common share[1]	**0.825**	0.765	0.705
Total assets	**4,970.6**	4,921.3	4,522.4
Long-term debt[2]	**2,166.6**	2,301.1	2,123.4
Current portion of long-term debt	**416.7**	51.8	108.9

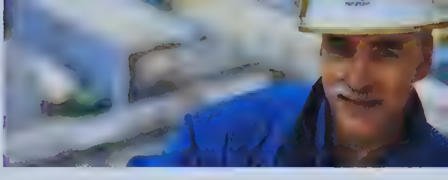
[1]*All per share amounts have been restated to reflect the 2-for-1 share split, which took effect in June 2004.*
[2]*Excluding current portion of long-term debt.*

Quarterly Financial Information

	Quarter Ended							
	2004				2003			
(dollars in millions except per share amounts)	**Dec.**	**Sept.**	**June**	**Mar.**	Dec.	Sept.	June	Mar.
Revenues	**$ 616.4**	**$ 327.1**	**$ 365.3**	**$ 648.2**	$ 615.7	$ 304.5	$ 400.4	$ 556.0
Earnings (loss) applicable to common shares								
Natural gas distribution								
Terasen Gas[1]	**$ 36.2**	**$ (13.3)**	**$ (1.2)**	**$ 48.0**	$ 37.5	$ (14.4)	$ (1.9)	$ 51.4
TGVI	**6.4**	**6.8**	**6.3**	**6.7**	7.3	7.1	5.8	6.0
	42.6	**(6.5)**	**5.1**	**54.7**	44.8	(7.3)	3.9	57.4
Petroleum transportation								
Trans Mountain	**11.2**	**8.8**	**9.0**	**10.4**	10.0	7.9	9.6	8.3
Corridor	**3.8**	**3.9**	**4.0**	**3.9**	4.0	3.8	2.9	—
Express System	**4.9**	**3.8**	**3.2**	**4.0**	3.9	2.8	(0.3)	3.3
	19.9	**16.5**	**16.2**	**18.3**	17.9	14.5	12.2	11.6
Water and utility services	**0.7**	**3.3**	**2.6**	**—**	0.4	2.2	2.1	(0.6)
Other activities	**(9.3)**	**(3.2)**	**(6.0)**	**(5.1)**	(8.8)	(5.9)	(3.6)	(4.7)
Earnings before non-recurring items	**53.9**	**10.1**	**17.9**	**67.9**	54.3	3.5	14.6	63.7
Non-recurring items	**—**	**—**	**—**	**—**	(3.4)	—	—	—
Earnings applicable to common shares	**$ 53.9**	**$ 10.1**	**$ 17.9**	**$ 67.9**	$ 50.9	$ 3.5	$ 14.6	$ 63.7
Per common share–basic[2]	**$ 0.51**	**$ 0.10**	**$ 0.17**	**$ 0.65**	$ 0.49	$ 0.03	$ 0.14	$ 0.62
Per common share–fully diluted[2]	**$ 0.51**	**$ 0.10**	**$ 0.17**	**$ 0.64**	$ 0.48	$ 0.03	$ 0.14	$ 0.61

[1]*Earnings from Terasen Gas have been restated to adjust for changes in the quarterly accounting for income tax. Previously, Terasen Gas' annual tax expense had been allocated based on income tax estimated to be collected in rates for the four quarters. Beginning in the fourth quarter of 2004, Terasen Gas' income tax expense is determined by applying the effective annual tax rate to the pre-tax income in the quarter. The change affects income tax expense and net earnings reported for each of the quarters but has no impact on annual income tax expense and net earnings.*

[2]*Earnings (loss) per share in each quarter have been determined based on the weighted average number of common shares outstanding during each quarter. The weighted average number of common shares outstanding was recalculated on a calendar year basis for annual results. Earnings (loss) per share by quarter do not necessarily add to the total of the year due to changes in the weighted average number of common shares outstanding during the year. All per share amounts have been restated to reflect the 2-for-1 share split, which took effect in June 2004.*



SEASONALITY

Because of natural gas consumption patterns, the natural gas distribution operations of Terasen Gas normally generate higher net earnings in the first and fourth quarters, which are offset by net losses in the second and third quarters. The Company's water and utility services business, which is relatively less significant than the Company's natural gas distribution operations, typically experiences stronger second and third quarter results, offset by weaker first and fourth quarter results, based on the level of construction and general economic activity. Earnings from Terasen's petroleum pipeline operations are not subject to material fluctuations due to seasonality. As a result, interim earnings statements are not indicative of earnings on an annual basis.

BUSINESS DEVELOPMENT

INLAND PACIFIC CONNECTOR

The Inland Pacific Connector is a proposed natural gas transmission line connecting the Southern Crossing pipeline to the Lower Mainland and Sumas. The advancement of the project is dependent on potential shippers and their requirements to diversify supply sources. The potential size of the project is $300 to $500 million.

VANCOUVER ISLAND GAS SUPPLY

TGVI is actively pursuing alternatives for the supply of additional natural gas capacity to Vancouver Island. The Company is responding to the need for delivery of increased gas supply and, accordingly, is supporting plans for new gas-fired power generation on Vancouver Island. TGVI's proposal for new natural gas capacity involves a combination of compression and pipeline looping as well as the addition of an LNG storage facility on Vancouver Island. The expansion costs are estimated at approximately $100 to $120 million for the additional compression and the new LNG storage facility. The proposed facility would have the capacity to hold one billion cubic feet of natural gas.

On February 16, 2005, the BCUC approved the LNG storage facility, subject to several conditions including the execution of a long-term Transportation Service Agreement (TSA) with B.C. Hydro. TGVI plans to work with B.C. Hydro and others to meet these conditions and proceed with the project, but there is no certainty that a TSA will ultimately be executed.

MUNICIPAL LEASING TRANSACTIONS

Certain municipalities in Terasen Gas' service area have an option to purchase the gas distribution franchise within their municipal boundary. In order to address these purchase options, the Company has developed a leasing arrangement that allows Terasen Gas to continue to operate the gas distribution assets by effectively selling the assets to the municipality and leasing them back for a 17 year period. After 17 years, Terasen Gas has an option to repurchase the assets at depreciated value. At December 31, 2004, Terasen Gas had entered into transactions involving a total value of $143 million. If all of the eligible municipalities execute similar transactions, the total value (including those already completed) is expected to be approximately $164 million.

ACQUISITION OF EXPRESS PIPELINE

On January 9, 2003, a consortium including Terasen, Borealis Infrastructure Management Inc., and Ontario Teachers' Pension Plan acquired the Express System from EnCana Corporation. The purchase price was $1,203.5 million, including assumed debt of $578.8 million. Terasen's share of the equity portion of the purchase price was $206.7 million. Each of the three consortium members owns an equal interest in the Express System. Terasen Pipelines operates the Express System on behalf of the consortium.

EXPANSION OF EXPRESS SYSTEM

During December 2003, Terasen held an open-season for current and expansion capacity on the Express System. Given the significant demand for capacity by the Shippers, Terasen, on behalf of the owners, is proceeding with both Phase I and Phase II of its expansion plans for the Express System. In total, the expansion will add 108,000 bpd in capacity, bringing the total capacity on the Express System to 280,000 bpd. Both phases of the expansion are expected to be completed by April 2005 at an estimated cost of approximately US$100 million. During July 2004, the Express partnership completed a long-term debt issue of US$110 million to finance the expansion.

TRANS MOUNTAIN EXPANSION

In 2004, Terasen completed an expansion of the Trans Mountain mainline that added an additional 27,000 bpd of capacity at a cost of $19 million. The expansion went into service on October 1, 2004.

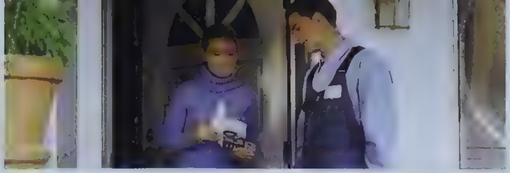
CORRIDOR EXPANSION/BISON PIPELINE PROJECT

Terasen has been working with Shell and its partners in the Athabasca Oil Sands Project toward expanding the Corridor Pipeline from 155,000 bpd to 300,000 bpd. Expansion of the system would be undertaken in phases, with the first phase consisting of de-bottlenecking the existing system by adding pumping capacity. This phase would increase capacity by approximately 35,000 bpd and would be in service by the fall of 2005. The estimated cost of phase one is $6.5 million. The scope of the phase one expansion has received approval from the Corridor Shippers' Committee. The second phase is under review and would expand the system by an additional 110,000 bpd. The estimated cost of this expansion is $500 to $600 million and is expected be in service by 2009. Terasen is also working on additional expansion opportunities, which would increase capacity on the Corridor system to 500,000 bpd. Such an expansion could provide the opportunity for spare capacity that could be used by third party shippers or made available for marketing to other oilsands producers.

TMX

During 2004, Trans Mountain continued development of TMX, the proposed staged expansion of the existing Trans Mountain system between Edmonton, Alberta and Burnaby, or the west coast of British Columbia. In 2004, the Company continued to develop the technical, regulatory and commercial components of the project. In December, Trans Mountain issued an expression of interest to solicit non-binding support for the project. With sufficient support the Company intends to finalize the commercial and tolling framework prior to holding an open season for binding commitments by mid-2005. Initial interim expansion capacity of 35,000 bpd could be available by the end of 2006 at a capital cost of $200 million, with a further 40,000 bpd available by the end of 2008 at an additional cost of $375 million (TMX1). TMX1 could be followed by additional expansions with total expenditures (including TMX1) of up to $2.2 to $2.6 billion, depending on the scale of the capacity required by shippers.

The staged approach to the proposed TMX expansion enables shippers to make progressive decisions, thereby reducing the overall risk to the producers and the pipeline. It also allows the shippers access to incremental expansion capacity in advance of making a decision on the southern or northern port option. Finally, the proposed southern routing for the TMX project follows much of the existing right-of-way for Trans Mountain pipeline, reducing the time, effort and cost required in securing access to the land. While the Company believes the TMX project offers a more attractive alternative to competing projects, ultimately it is the shipper's commitments that will determine the successful project.



Project development expenditures for TMX in 2004 totaled $3.8 million. The Company expects to spend an additional $7 to $12 million prior to receiving binding support for the project.

ACQUISITION OF FAIRBANKS SEWER AND WATER

On July 31, 2004, Terasen acquired a 50 per cent interest in Fairbanks Sewer and Water Inc. FSW provides water and wastewater treatment and water distribution and wastewater collection services to Fairbanks, Alaska, an area of 82,000 residents. The Company paid $40.8 million (US$30.5 million) for its 50 per cent interest, and Terasen and the current owners each have the option to have Terasen acquire the remaining 50 per cent at fair market value in 2009. FSW is regulated by the Regulatory Commission of Alaska.

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

Terasen's critical accounting policies are defined as those that are both significant to the representation of the Company's financial position and operations and those that require management to make judgments based on underlying estimates and assumptions about future events and their effects. Underlying estimates and assumptions are based on historical experience and other factors that management believes to be reasonable and prudent under the circumstances. These estimates and assumptions are subject to change as new events occur, as more industry experience is acquired, as additional information is obtained and as the general operating environment changes. The Company believes the following are the most critical accounting policies and estimates used in the preparation of its consolidated financial statements.

RATE REGULATION

The Company follows generally accepted accounting principles, which may differ for regulated operations from those otherwise expected in non-regulated businesses. These differences occur when the regulatory agencies render their decisions on rate applications and generally involve the timing of revenue and expense recognition to ensure that the actions of the regulator, which create assets and liabilities, have been reflected in the financial statements.

The accounting for these items is based on an expectation of the future actions of the regulator. For example, Terasen Gas does not record future income taxes related to its regulated operations as the taxes payable method is prescribed by the regulator for rate-making purposes and there is reasonable expectation that all such future income taxes will be recovered in rates when they become payable. Similarly, the deferral of differences between amounts included in rates and actual experience for specified expenses is based on the expectation that the regulator will approve the refund to or recovery from ratepayers of the deferred balance, normally in the following year.

If the regulator's future actions are different from the Company's expectations, the timing and amount of the recovery of liabilities or refund of assets, recorded or unrecorded, could be substantially different from that reflected in the financial statements.

DEPRECIATION EXPENSE

Terasen's regulated property, plant and equipment assets are depreciated on a straight-line basis at rates approved by regulatory authorities. Depreciation rates require the use of management estimates of the useful lives of the assets. The cost of depreciable property retired, together with the removal costs less salvage, are recoverable based on the cost of providing the products or services. The Company's non-regulated property, plant and equipment assets are depreciated according to their estimated useful life.

CHANGES IN ACCOUNTING POLICIES

FINANCIAL INSTRUMENTS

Effective January 1, 2005, the Canadian Institute of Chartered Accountants (CICA) amended Section 3860 "Financial Instruments – Disclosure and Presentation", which requires obligations that can be settled at the issuer's option by a variable number of the issuer's own equity instruments to be presented as liabilities. This amendment will require Terasen to retroactively classify $125.0 million of capital securities as debt rather than as a component of shareholder's equity, with an annual pre-tax expense of $10 million to be recorded as financing costs, as opposed to a direct charge to retained earnings. There is no impact on earnings per share or earnings applicable to common shares.

VARIABLE INTEREST ENTITIES

The CICA has adopted Accounting Guideline 15 "Consolidation of Variable Interest Entities", which requires entities to consolidate those companies in which it holds a significant interest if it meets certain risk and reward criteria. On January 4th, 2005, Terasen Gas unwound its Coastal Facilities lease agreement and the assets have been included in the Terasen Gas rate base commencing January 2005.

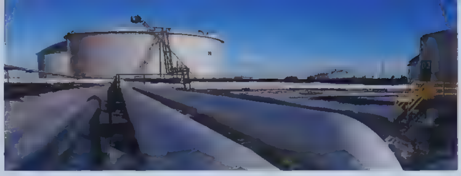
RATE REGULATED ENTITIES

In 2003 the CICA reintroduced proposals to develop accounting standards for rate regulated enterprises which could have a significant impact on the Company's regulated operations. Although the CICA continues to deliberate on recognition and measurement issues related to rate regulation, in September 2004 the CICA issued a draft Guideline for comment on disclosures by entities with rate regulated operations. The proposed Guideline addresses certain aspects of disclosure and presentation of information in the financial statements of entities which have rate-regulated operations. The proposed disclosures are comprised of general information that facilitates an understanding of the effects of rate regulation on an entity's financial statements and additional information on how specific financial statement items have been affected. If approved, the draft guideline could be effective for annual and interim periods beginning on or after April 1, 2005.

ASSET RETIREMENT OBLIGATIONS

On January 1, 2004, the Company adopted the new CICA standard for recognition, measurement and disclosure of liabilities for asset retirement obligations and the associated asset retirement costs. Under the new standard the fair value of a liability for an asset retirement obligation must be recognized in the period in which it is incurred if a reasonable estimate of fair value can be made. The fair value is added to the carrying amount of the associated asset, which is then expensed over the asset's estimated useful life. The liability is accreted over the estimated useful life of the asset through charges to expenses.

As the fair value of future removal and site restoration costs is not currently determinable, the adoption of this policy does not result in the recording of an asset retirement liability and therefore the financial statements have not been impacted by this new standard. In addition, for regulated operations there is a reasonable expectation that asset retirement costs would be recoverable through future rates.



HEDGING RELATIONSHIPS

Effective January 1, 2004, the Company adopted the new accounting guideline on hedging relationships which specifies the circumstances in which hedge accounting is appropriate, including the identification, documentation, designation, and effectiveness of hedges. The guideline also identifies situations where hedge accounting is to be discontinued. The Company has met the criteria for all designated hedging relationships. The accounting treatment for financial instruments substantially conforms with those used in the Company's most recent annual consolidated financial statements.

FORWARD LOOKING STATEMENT

When used in this report, the words "anticipate", "expect", "project", "believe", "estimate", "forecast" and similar expressions are intended to identify forward looking statements, which include statements relating to pending and proposed projects or possible acquisitions. Such statements are subject to certain risks, uncertainties and assumptions pertaining to operating performance, regulatory parameters, economic conditions and, in the case of pending and proposed projects, risks relating to design and construction, regulatory processes, obtaining financing and performance of other parties, including partners, contractors and suppliers and in the case of possible acquisitions, obtaining financing, acquiring assets or companies at an appropriate price and the ability to effect synergies in a timely and cost-effective manner.

ADDITIONAL INFORMATION

Additional information relating to Terasen Inc., including its Annual Information Form, is available on SEDAR at www.sedar.com.

Management's Responsibility

The consolidated financial statements have been prepared by management, which is responsible for the integrity and objectivity of this information. These financial statements have been prepared in conformity with Canadian generally accepted accounting principles and, where appropriate, include amounts that are based on management's best estimates and judgments. The financial information presented elsewhere in the annual report is consistent with that in the consolidated financial statements.

Management has established systems of internal control which are designed to provide reasonable assurance that assets are safeguarded from loss and that reliable financial records are maintained. These systems are monitored by internal auditors.

KPMG LLP, the independent auditors appointed by the shareholders, have audited the consolidated financial statements of the Company in accordance with Canadian generally accepted auditing standards and have expressed their opinion upon completion of such audits in the following report. In order to provide their opinion on these consolidated financial statements, the shareholders' auditors review the system of internal controls and conduct their work to the extent they consider appropriate.

The Board of Directors, through its Audit Committee, oversees management's responsibilities for financial reporting and internal control. The Audit Committee meets with the internal auditors, the independent auditors and management to discuss auditing and financial matters and to review the consolidated financial statements and the independent auditors' report. The Audit Committee reports its findings to the Board for consideration in approving the consolidated financial statements for issuance to the shareholders.

J. M. Reid

John M. Reid
President and Chief Executive Officer

Gordon Barefoot

Gordon R. Barefoot
Senior Vice President, Finance, and Chief Financial Officer

Vancouver, Canada
February 2, 2005

Auditors' Report To The Shareholders

We have audited the consolidated statements of financial position of Terasen Inc. as at December 31, 2004 and 2003 and the consolidated statements of earnings, retained earnings and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 2004 and 2003 and the results of its operations and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

KPMG LLP

Chartered Accountants

Vancouver, Canada
February 2, 2005

Consolidated Statements of Earnings

In millions of dollars, except per share data

Years ended December 31	2004	2003
Revenues		
Natural gas distribution	$ 1,494.1	$ 1,497.9
Petroleum transportation	225.5	200.0
Water and utility services	201.6	152.5
Other activities	35.8	26.2
	1,957.0	1,876.6
Expenses		
Cost of natural gas	885.4	889.7
Cost of revenues from water and utility services and other activities	174.3	132.4
Operation and maintenance	302.9	284.8
Depreciation and amortization	147.1	133.4
Property and other taxes	70.1	69.9
	1,579.8	1,510.2
Operating income	377.2	366.4
Financing costs (note 14)	166.6	176.0
Earnings before share of earnings of Express System and income taxes	210.6	190.4
Share of earnings of Express System (note 3)	15.0	8.0
Earnings before income taxes	225.6	198.4
Income taxes (note 15)	69.2	59.0
NET EARNINGS	156.4	139.4
Capital securities distributions, net of income taxes (note 11)	6.6	6.7
EARNINGS APPLICABLE TO COMMON SHARES	$ 149.8	$ 132.7
Common shares – weighted average (millions)	104.7	103.8
BASIC EARNINGS PER COMMON SHARE (note 11)	$ 1.43	$ 1.28
DILUTED EARNINGS PER COMMON SHARE (note 11)	$ 1.42	$ 1.27

Consolidated Statements of Retained Earnings

In millions of dollars

Years ended December 31	2004	2003
Retained earnings, beginning of year	$ 355.5	$ 302.2
Net earnings	156.4	139.4
	511.9	441.6
Dividends on common shares	86.4	79.4
Capital securities distributions, net of income taxes	6.6	6.7
	93.0	86.1
Retained earnings, end of year	$ 418.9	$ 355.5

Consolidated Statements of Financial Position

In millions of dollars

As at December 31	**2004**	2003
Assets		
Current assets		
Cash and short-term investments	**$ 20.0**	$ 1.5
Accounts receivable	**348.6**	404.3
Inventories of gas in storage and supplies	**189.2**	142.4
Prepaid expenses	**11.2**	13.4
Current portion of rate stabilization accounts (note 7)	**27.1**	21.6
	596.1	583.2
Property, plant and equipment (note 6)	**3,892.5**	3,882.4
Investment in Express System (note 3)	**218.9**	204.6
Goodwill	**128.0**	101.9
Rate stabilization accounts (note 7)	**60.6**	75.7
Other assets (note 8)	**74.5**	73.5
	$ 4,970.6	$ 4,921.3
Liabilities and Shareholders' Equity		
Current liabilities		
Short-term notes	**$ 248.0**	$ 553.9
Accounts payable and accrued liabilities	**369.8**	369.6
Income and other taxes payable	**36.4**	43.9
Current portion of rate stabilization accounts (note 7)	**27.6**	6.2
Current portion of long-term debt (note 9)	**416.7**	51.8
	1,098.5	1,025.4
Long-term debt (note 9)	**2,166.6**	2,301.1
Other long-term liabilities and deferred credits (note 10)	**140.7**	99.8
Future income taxes (note 15)	**68.7**	67.5
	3,474.5	3,493.8
Shareholders' equity		
Capital securities (note 11)	**125.0**	125.0
Common shares (note 11)	**883.4**	868.7
Contributed surplus (note 11)	**132.5**	131.4
Retained earnings	**418.9**	355.5
Cumulative currency translation adjustment	**(12.7)**	(2.1)
	1,547.1	1,478.5
Less cost of common shares held by Terasen Pipelines (Trans Mountain) Inc.	**51.0**	51.0
	1,496.1	1,427.5
	$ 4,970.6	$ 4,921.3

Approved by the Board:

Mark L. Cullen
Director

John M. Reid
Director

Consolidated Statements of Cash Flows

In millions of dollars

Years ended December 31	2004	2003
Cash flow provided by (used for)		
Operating activities		
Net earnings	$ 156.4	$ 139.4
Adjustments for non-cash items		
Depreciation and amortization	147.1	133.4
Share of earnings from Express System, net of (in excess of) cash distributions	(14.3)	2.1
Future income taxes	(0.5)	9.4
Other	7.6	5.0
	296.3	289.3
Decrease in rate stabilization accounts	31.0	50.7
Changes in non-cash working capital	14.7	(70.2)
	342.0	269.8
Investing activities		
Property, plant and equipment	(154.4)	(222.9)
Acquisition of water and utility services businesses (note 3)	(57.9)	—
Acquisition of Express System (note 3)	—	(206.7)
Proceeds on sale of natural gas distribution assets (note 10)	64.6	—
Proceeds on sale of other property, plant and equipment	0.9	—
Other assets	(13.4)	(2.3)
	(160.2)	(431.9)
Financing activities		
Increase (decrease) in short-term notes	(305.9)	113.9
Increase in long-term debt	339.1	461.4
Reduction of long-term debt	(118.2)	(340.8)
Issue of common shares, net of issue costs (note 11)	14.7	10.1
Dividends and distributions on common shares and capital securities	(93.0)	(86.1)
	(163.3)	158.5
Net increase (decrease) in cash	18.5	(3.6)
Cash at beginning of year	1.5	5.1
Cash at end of year	$ 20.0	$ 1.5
Supplemental cash flow information		
Interest paid in the year	$ 162.7	$ 184.7
Income taxes paid in the year	78.1	47.9

Cash is defined as cash or bank indebtedness.

Tabular amounts in millions of dollars, except where stated otherwise
Years ended December 31, 2004 and 2003

Terasen Inc. ("Terasen" or the "Company") provides energy transportation and utility asset management services. Terasen operates in three primary business segments which are separately managed to assess operational performance.

(a) Natural gas distribution operations involve the transmission and distribution of natural gas and propane for residential, commercial, institutional, and industrial customers in British Columbia. The operations are conducted through Terasen Gas Inc. ("Terasen Gas"), serving the Lower Mainland and interior of British Columbia, Terasen Gas (Vancouver Island) Inc. ("TGVI"), serving Vancouver Island and the Sunshine Coast, Terasen Gas (Whistler) Inc., and Terasen Gas (Squamish) Inc.

(b) Petroleum transportation operations are carried out through Terasen Pipelines (Trans Mountain) Inc. ("Trans Mountain"), which owns and operates a common carrier pipeline system for crude and refined petroleum products transported from Edmonton, Alberta to Vancouver, British Columbia and Washington State, Terasen Pipelines (Corridor) Inc. ("Corridor"), a pipeline in northern Alberta transporting diluted bitumen, and the one-third owned entities Express Pipeline LP and Express US Holdings LP ("the Express System"). The Express System transports crude oil from Hardisty, Alberta, through the Rocky Mountain region of the United States and on to Wood River, Illinois.

(c) Water and utility services operations includes providing water and wastewater treatment services, water distribution and wastewater collection, meter reading, meter fleet management and installation services as well as product sales related to the water, sewer and irrigation markets. These operations are provided through Terasen Waterworks (Supply) Inc., Terasen Utility Services Inc., Terasen Utility Services (U.S.) Inc. (collectively "Terasen Water and Utility Services"), the Company's 50% interest in Fairbanks Sewer and Water Inc. ("FSW") and the Company's 30% interest in CustomerWorks LP ("CWLP").

(d) Other activities include international consulting activities, the Company's 45% (2003–44%) proportionate interest in Clean Energy Fuels Corp. ("Clean Energy") and corporate financing costs and administration charges.

The Company operates in Canada and the United States, but at the present time the United States operations are not of sufficient size to be reportable as either operating or geographic segments.

On April 25, 2003, the Company changed its name from BC Gas Inc. to Terasen Inc.

1. Significant Accounting Policies

The preparation of these consolidated financial statements in conformity with Canadian generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses in the financial statements, as well as the disclosure of contingent assets and liabilities. Actual results could differ from those estimates.

In the opinion of management, these consolidated financial statements have been properly prepared within reasonable limits of materiality and reflect the following summary of significant accounting policies.

Basis of Presentation

The consolidated financial statements include the accounts of the Company, its subsidiaries, and its proportionate share of the accounts of jointly-controlled entities. Investments in entities which are not subsidiaries or joint ventures, but over which the Company exercises significant influence, are accounted for using the equity method.

Certain of the prior year comparative figures have been reclassified to conform with the current year's presentation.

Foreign Currency Translation

The Company translates its self-sustaining U.S. dollar denominated water and utility service businesses' and Clean Energy's financial statements into Canadian dollars using the current rate method of foreign currency translation. Under this method, assets and liabilities are translated at the rate of exchange in effect at the balance sheet date, revenue and expense items are translated at average rates of exchange for the period, and the exchange gains and losses arising on the translation of the financial statements are recorded in the cumulative currency translation adjustment account in Shareholders' equity.

The Company's U.S.-based petroleum transportation operations are integrated and are translated into Canadian dollars using the temporal method. Under this method, monetary assets and liabilities denominated in foreign currencies are translated at exchange rates in effect at the balance sheet date, with the exception of certain long-term debt in the Express System, which is considered to be a hedge of U.S. dollar denominated revenues in the Express System. Non-monetary assets and liabilities denominated in foreign currencies are translated at exchange rates in effect on the dates the assets were acquired or liabilities assumed. Revenues and expenses are translated at the average rates of exchange prevailing during the month the transactions occurred. Under this method, exchange gains and losses on translation are reflected in income when incurred.

Regulation

The natural gas distribution companies are subject to the regulation of the British Columbia Utilities Commission ("the BCUC"). The Trans Mountain and Express System operations are governed by contractual arrangements with shippers and are regulated in Canada by the National Energy Board and, in the United States, tariff matters are regulated by the Federal Energy Regulatory Commission.

Corridor's operations are governed by contractual arrangements with shippers and are subject to regulation by the Alberta Energy and Utilities Board ("the AEUB"). FSW is regulated by the Regulatory Commission of Alaska.

These regulatory authorities exercise statutory authority over such matters as rates of return, construction and operation of facilities, accounting practices, rates and tolls, and contractual agreements with customers.

In order to recognize the economic effects of regulation, the timing of recognition of certain revenues and expenses in these operations may differ from that otherwise expected under generally accepted accounting principles for non-regulated businesses.

Inventories

Inventories of gas in storage are valued at weighted-average cost. Supplies and other inventories are valued at the lower of cost and net realizable value.

Property, Plant and Equipment

Property, plant and equipment are recorded at cost less accumulated depreciation and unamortized contributions in aid of construction. Cost includes all direct expenditures for system expansions, betterments and replacements, an allocation of overhead costs and an allowance for funds used during construction. When allowed by the regulators, regulated operations capitalize an allowance for equity funds used during construction at approved rates.

Depreciation of regulated assets is recorded on a straight-line basis over their useful lives. Depreciation rates for regulated assets are approved by the respective regulator, and for non-regulated assets requires the use of management estimates of the useful lives of assets. Depreciation of nonregulated equipment is recorded using the declining balance method.

The cost of regulated depreciable property retired, together with removal costs less salvage, is charged to accumulated depreciation, as is any gain or loss incurred on disposal.

Impairment of Long-Lived Assets

On January 1, 2004, the Company adopted the Canadian Institute of Chartered Accountants ("CICA") standard for recognizing, measuring and disclosing impairment of long-lived assets held for use. A long-lived asset is tested for recoverability when events or changes in circumstances indicate that its carrying amount may not be recoverable. The new standard has had no impact on the Company's financial results.

Asset Retirement Obligations

On January 1, 2004, the Company adopted the new CICA standard for the recognition, measurement and disclosure of liabilities for asset retirement obligations and the associated asset retirement costs. Under the new standard the fair value of a liability for an asset retirement obligation must be recognized in the period in which it is incurred if a reasonable estimate of fair value can be made. The fair value is added to the carrying amount of the associated long-lived asset, which is then expensed over the asset's estimated useful life. The liability is accreted over the useful life of the asset through charges to expenses.

As the fair value of future removal and site restoration costs is not currently determinable, the adoption of the policy does not result in the recording of an asset retirement liability and therefore the financial statements have not been impacted by the new standard. In addition, for regulated operations there is a reasonable expectation that asset retirement costs would be recoverable through future rates or tolls.

Rate Stabilization Accounts

TGVI maintains a BCUC approved Revenue Deficiency Deferral Account ("RDDA") to accumulate unrecovered costs of providing service to customers or to drawdown such costs where earnings exceed an allowed return as set by the BCUC. The RDDA has accumulated the allowed earnings in excess of achieved earnings prior to 2003 and is to be recovered through future rates. During the years ended December 31, 2004 and 2003, the RDDA has decreased as achieved earnings have exceeded the allowed return.

Terasen Gas is authorized by the BCUC to maintain rate stabilization accounts to mitigate the effect on its earnings of unpredictable and uncontrollable factors, namely volume volatility caused principally by weather and natural gas cost volatility. The Revenue Stabilization Adjustment Mechanism ("RSAM") accumulates the margin impact of variations in the actual versus forecast volume use for residential and commercial customers.

In 2004, the Gas Cost Reconciliation Account ("GCRA"), which accumulates differences between actual natural gas costs and forecast natural gas costs as recovered in base rates, was replaced by the Commodity Cost Reconciliation Account ("CCRA") and the Midstream Cost Reconciliation Account ("MCRA"). The two new accounts were approved by the BCUC to segregate costs that are allocable to all sales customers (MCRA) and all residential customers and certain commercial and industrial customers for whom Terasen Gas acquires gas supply (CCRA).

All rate stabilization account balances for both TGVI and Terasen Gas are amortized and recovered through rates as approved by the BCUC.

Deferred Charges

The Company defers certain costs which the regulatory authorities or contractual arrangements require or permit to be recovered through future rates or tolls. Deferred charges are amortized over various periods as approved by the regulator and depending on the nature of the costs.

Deferred charges include long-term debt issue costs which are amortized over the term of the related debt.

Deferred charges not subject to regulation relate to projects which may benefit future periods and will be capitalized on completion, expensed on project abandonment, or are being amortized on a straight-line basis over their useful lives.

Goodwill

Goodwill represents the excess of an investment over the fair value of the net assets acquired. Goodwill is not amortized and is tested annually for impairment by comparing the book value with the fair value of the goodwill of the reporting unit to which the goodwill is attributable. Any deficiency in the book value compared to the fair value will be recognized as an impairment loss.

Revenue Recognition

The Company recognizes revenues when products have been delivered or services have been performed.

The natural gas distribution utilities record revenues from natural gas sales on the basis of regular meter readings and estimates of customer usage since the last meter reading date to the end of the year and adjusted for the Revenue Stabilization Adjustment Mechanism and other BCUC-approved orders.

For the petroleum transportation operations, revenues are recorded when products are delivered and adjusted according to terms prescribed by toll settlements with the shippers and approved by the respective regulator.

For the water and utility services operations revenues are recorded when services have been performed or products have been delivered.

Derivative Financial Instruments

The Company utilizes derivatives and other financial instruments to manage its exposure to changes in foreign currency exchange, interest rates and energy commodity prices.

A derivative must be designated and effective to be accounted for as a hedge. The Company designates each derivative instrument as a hedge of specific assets or liabilities on the balance sheet, specific firm commitments or anticipated transactions. The Company also assesses, both at inception and on an ongoing basis, whether the derivative instruments that are used in each hedging transaction are highly effective in offsetting changes in fair values or cash flows of the hedged items.

The Company formally documents all relationships between hedging instruments and hedged items, as well as its risk management objective and strategy for undertaking various hedge transactions.

As approved by the regulator, derivatives are used to manage natural gas commodity price risk in the natural gas distribution operations. The majority of natural gas supply contracts have floating, rather than fixed prices. The Company uses natural gas price swap contracts to fix the effective purchase price. Any differences between the effective cost of natural gas purchased and the price of natural gas included in rates are recorded in deferral accounts (CCRA and MCRA), and subject to regulatory approval, are passed through in future rates to customers.

The Company's short-term borrowings and variable rate long-term debt are exposed to interest rate risk. The Company manages interest rate risk through the use of interest rate derivatives with payments and receipts under interest rate swap contracts being recognized as adjustments to financing costs.

Foreign currency risk in natural gas distribution operations relates mainly to purchases and sales of natural gas denominated in U.S. dollars, and is thereby managed through regulatory deferral accounts. Certain foreign currency risks in the natural gas distribution operations are managed on behalf of customers through the use of foreign currency derivatives.

The Company's earnings from the U.S. portion of Trans Mountain's crude oil pipeline system and the Company's investment in the Express System are subject to foreign currency risk. The Company's earnings are also subject to translation risk associated with certain Express System assets and liabilities. The Company manages some of these foreign currency exposures through the use of foreign currency derivatives.

Unless otherwise approved by regulation, if a derivative instrument is terminated or ceases to be effective prior to maturity, the gain or loss at that date is deferred and recognized in income concurrently with the hedged item. Any subsequent changes in the value of the derivative instrument are reflected in income.

Non-hedge derivatives are marked to market at the balance sheet date with fluctuations in value charged to earnings.

Post-Employment Benefit Plans

The Company sponsors a number of employee benefits plans. These plans include both defined benefit and defined contribution pension plans, and various other post-retirement benefit plans.

The cost of pensions and other post-retirement benefits earned by employees is actuarially determined as the employee provides service, except when the regulator requires costs to be expensed as paid. The Company uses the projected benefit method based on years of service and management's best estimates of expected returns on plan assets, salary escalation, retirement age of employees, mortality and expected future health-care costs. The discount rate used to value liabilities is based on AA Corporate bond yields. The Company accrues the cost of defined benefit pensions and post-employment benefits as the employee provides services, except when the regulator requires costs to be expensed as paid.

The expected return on plan assets is based on management's estimate of the long-term expected rate of return on plan assets and a market-related value of plan assets. The market-related value of assets as of December 31, 2004 is calculated as the average of the market value of invested assets at December 31, 2004 and two actuarially determined extrapolated market values of invested assets at December 31, 2004. The two extrapolated market values are calculated by using the market value of invested assets at December 31, 2002 rolled forward to December 31, 2004 using 2003 and 2004 net contributions and assumed investment returns, and the market value of invested assets at December 31, 2003 rolled forward to December 31, 2004 using 2004 net contributions and assumed investment returns. These three amounts are then averaged to determine the market-related value of plan assets used in calculating net benefit expense.

Adjustments, in excess of 10% of the greater of the accrued benefit obligation and plan asset fair value, that result from plan amendments, changes in assumptions and experience gains and losses are amortized over the expected average remaining service life of the employee group covered by the plan. Experience will often deviate from the actuarial assumptions resulting in actuarial gains and losses.

Defined contribution plan costs are expensed by the Company as contributions are payable.

Income Taxes

The Company's regulated gas and petroleum operations account for and recover income tax expense in rates as prescribed by their respective regulators. This includes accounting for income taxes by the taxes payable method and accounting for certain deferral and rate stabilization accounts on a net of realized tax basis. Therefore, future income taxes related to temporary differences are not recorded. The taxes payable method is followed as there is a reasonable expectation that all future income taxes will be recovered in rates when they become payable.

The Company's non-regulated operations and FSW follow the asset and liability method of accounting for income taxes. Future income tax assets and liabilities are determined based on temporary differences between the tax bases of assets and liabilities and their carrying values for accounting purposes. Future income tax assets and liabilities are measured at the tax rate that is expected to apply when the temporary differences reverse.

Stock-Based Compensation

The Company has a Share Option Plan whereby officers, directors and certain key employees may be granted options to purchase common shares. The Company uses the fair value based method for valuing stock options granted on or after January 1, 2003. Under the fair value based method, compensation cost is measured at the fair value at the date of grant and is expensed over the award's vesting period.

Prior to January 1, 2003, the Company used the settlement method of accounting for stock options, whereby any consideration paid by employees on the exercise of stock options was credited to common shares and no compensation expense was recognized.

The Company has issued Deferred Share Units ("DSU's") to senior management and Board members under long-term compensation programs and also as an optional form of compensation to Board members. The DSU's are marked-to-market at the end of each quarter and gains or losses are recognized in earnings. The DSU's notionally earn dividends that are reinvested as additional DSU's when dividends are paid, and are paid out in cash only on retirement or termination of the individual receiving them.

2. Segment Disclosures

2004	Natural gas distribution	Petroleum transportation	Water and utility services	Other activities	Total
Revenues	$ 1,494.1	$ 225.5	$ 201.6	$ 35.8	$ 1,957.0
Cost of natural gas	885.4	—	—	—	885.4
Cost of revenues from water and utility services and other activities	—	—	152.4	21.9	174.3
Operation and maintenance	190.5	66.0	28.3	18.1	302.9
Depreciation and amortization	98.7	35.9	9.3	3.2	147.1
Property and other taxes	47.1	22.5	0.2	0.3	70.1
	1,221.7	124.4	190.2	43.5	1,579.8
Operating income	272.4	101.1	11.4	(7.7)	377.2
Financing costs	126.2	22.5	1.0	16.9	166.6
Share of (earnings) of Express System	—	(15.0)	—	—	(15.0)
Income taxes (recovery) on earnings	50.3	22.7	3.8	(7.6)	69.2
Net earnings (loss)	95.9	70.9	6.6	(17.0)	156.4
Earnings (loss) applicable to common shares	95.9	70.9	6.6	(23.6)	149.8
Earnings (loss) per common share	0.92	0.68	0.06	(0.23)	1.43
Total assets	3,375.0	1,350.4	186.7	58.5	4,970.6
Goodwill	76.5	—	40.8	10.7	128.0
Capital expenditures	112.3	31.0	7.8	3.3	154.4

2003	Natural gas distribution	Petroleum transportation	Water and utility services	Other activities	Total
Revenues	$ 1,497.9	$ 200.0	$ 152.5	$ 26.2	$ 1,876.6
Cost of natural gas	889.7	—	—	—	889.7
Cost of revenues from water and utility services and other activities	—	—	115.4	17.0	132.4
Operation and maintenance	189.4	57.0	21.4	17.0	284.8
Depreciation and amortization	92.5	30.0	8.0	2.9	133.4
Property and other taxes	48.6	21.0	0.1	0.2	69.9
	1,220.2	108.0	144.9	37.1	1,510.2
Operating income	277.7	92.0	7.6	(10.9)	366.4
Financing costs	135.5	23.2	0.9	16.4	176.0
Share of (earnings) of Express System	—	(8.0)	—	—	(8.0)
Income taxes (recovery) on earnings	46.8	20.6	2.6	(11.0)	59.0
Net earnings (loss)	95.4	56.2	4.1	(16.3)	139.4
Earnings (loss) applicable to common shares	95.4	56.2	4.1	(23.0)	132.7
Earnings (loss) per common share	0.92	0.54	0.04	(0.22)	1.28
Total assets	3,422.6	1,337.6	115.7	45.4	4,921.3
Goodwill	76.5	—	12.0	13.4	101.9
Capital expenditures	135.1	77.2	10.1	0.5	222.9

The segmented disclosures in these consolidated financial statements have been changed from those reported in the December 31, 2003 annual financial statements and now include the water and utility services business as a separate reportable segment which was previously included in other activities. This segment includes Terasen Water and Utility Services as well as Terasen's 50% share of FSW and 30% share of CWLP. The comparative segment information has been restated to reflect this change.

3. Acquisitions and Related Financings

Water and Utility Services Acquisitions

On July 31, 2004, the Company acquired a 50 per cent interest in FSW. FSW provides water and wastewater treatment and water distribution and wastewater collection services to Fairbanks, Alaska. The Company paid $40.8 million for its 50 per cent interest after working capital adjustments. The Company has accounted for the acquisition of FSW using the purchase method and has proportionately consolidated its 50 per cent of operations since the date of acquisition.

The Company and the other owners of FSW each have the option to have Terasen acquire the remaining 50 per cent interest in FSW at fair market value in 2009.

During 2004, the Company also acquired 100 per cent of two businesses and increased its investment in two other businesses that provide meter reading, meter fleet management and installation services in Canada and the United States. The Company paid $17.1 million for the interest in these businesses after working capital adjustments. The earnings of these acquired businesses have been included in the statement of earnings from the date of acquisition.

The following table provides the allocation of the purchase price over the assets and liabilities acquired:

	FSW	Other	Total
Working capital	$ 2.2	$ 7.1	$ 9.3
Property, plant and equipment	27.0	1.6	28.6
Goodwill	24.0	8.0	32.0
Other assets	0.5	0.4	0.9
Future income taxes	(2.0)	—	(2.0)
Long-term debt assumed	(10.9)	—	(10.9)
Total cash paid	$ 40.8	$ 17.1	$ 57.9

Express System

On January 9, 2003, a consortium including the Company, Borealis Infrastructure Management Inc. and the Ontario Teachers' Pension Plan Board acquired the Express Group of companies, which includes Express Pipeline LP. and Express Holdings (U.S.A.) LP. from EnCana Corporation. Each of the three consortium members owns an equal interest in the Express System. The total purchase price was $1,203.5 million, including assumed debt of $578.8 million. The Company's share of the purchase price was $206.7 million.

The Company exercises significant influence over the Express System and, accordingly, accounts for its one-third investment in the Express System using the equity method. Under the equity method the investment has been initially recorded at cost, and is subsequently adjusted to recognize the Company's share of earnings of the Express System and is reduced by distributions.

4. Restructuring

During the year ended December 31, 2003, the Company's natural gas distribution operations undertook a management and administrative restructuring and integration. The initiative was undertaken to generate efficiencies and harmonize processes and systems between Terasen Gas and TGVI. As a result of the restructuring, natural gas distribution operations recorded a charge of $3.4 million in 2003 and $0.7 million in 2004, net of previously recorded accruals, tax and the deferral of an amount for future recovery from customers through rates. The pre-tax charges have been included in operations and maintenance expense.

5. Investments in Jointly-Controlled Entities

The Company has a 50% interest in FSW, a 45% interest in Clean Energy and a 30% interest in CWLP for which it uses the proportionate consolidation method of accounting. The Company's proportionate share of assets, liabilities, revenues, expenses, and cash flows related to these entities is summarized as follows:

	2004	2003
Current assets	$ 27.1	$ 20.4
Long-term assets (including property, plant and equipment and goodwill)	121.0	80.6
Current liabilities	41.3	29.8
Long-term liabilities	20.4	8.7
Revenues	77.7	60.7
Expenses (including financing costs and income tax)	71.8	58.7
Net income	5.9	2.0
Cash flows from operating activities	7.8	26.7
Cash flows from investing activities	(7.5)	(7.6)
Cash flows from financing activities	0.2	(1.8)

6. Property, Plant and Equipment

2004	Weighted average depreciation rate	Cost	Accumulated depreciation	Net book value
Natural gas distribution	2.40%	$ 3,009.6	$ 542.5	$ 2,467.1
Petroleum pipeline systems	2.51%	1,295.0	295.9	999.1
Water and utility plant and distribution systems	3.71%	34.0	1.8	32.2
Plant, buildings and equipment	8.98%	404.4	160.3	244.1
Land and land rights	0.25%	152.6	2.6	150.0
		$ 4,895.6	$ 1,003.1	$ 3,892.5

2003	Weighted average depreciation rate	Cost	Accumulated depreciation	Net book value
Natural gas distribution	2.36%	$ 2,979.2	$ 486.7	$ 2,492.5
Petroleum pipeline systems	2.54%	1,260.0	265.6	994.4
Water and utility plant and distribution systems	6.01%	5.2	1.0	4.2
Plant, buildings and equipment	8.47%	404.6	153.2	251.4
Land and land rights	0.23%	141.8	1.9	139.9
		$ 4,790.8	$ 908.4	$ 3,882.4

7. Rate Stabilization Accounts

		2004		2003
Current Assets				
RDDA	$	12.9	$	12.8
RSAM		11.1		8.8
GCRA		2.7		–
Gas Cost Variance Account (TGVI)		0.4		–
		27.1		21.6
Long-Term Assets				
RDDA		32.7		43.5
RSAM		27.9		32.2
		60.6		75.7
Current Liabilities				
MCRA		(27.6)		–
GCRA		—		(2.5)
Gas Cost Variance Account (TGVI)		—		(3.7)
		(27.6)		(6.2)
Net rate stabilization accounts	$	60.1	$	91.1

The current portion of the rate stabilization accounts represents the amounts expected to be recovered in rates over the next twelve months. Actual recoveries will vary depending on actual natural gas consumption and recovery amounts approved by the BCUC.

The RSAM account is anticipated to be recovered in rates over three years. Recovery of the RSAM balance is dependent upon annually approved rates and actual gas consumption volumes. The MCRA and CCRA accounts, which succeeded the GCRA account in 2004, are anticipated to be fully recovered or paid within the next fiscal year.

8. Other Assets

		2004		2003
Deferred charges				
Regulated	$	46.2	$	47.9
Non-regulated		13.7		13.8
Investments		1.3		2.6
Long-term receivables		13.3		9.2
	$	74.5	$	73.5

9. Long-Term Debt

	2004	2003
Terasen Inc.		
(a) Medium Term Note Debentures:		
6.30% Series 1, due December 1, 2008	**$ 200.0**	$ 200.0
4.85% Series 2, due May 8, 2006	**100.0**	100.0
5.56% Series 3, due September 15, 2014	**125.0**	—
	425.0	300.0
Terasen Gas Inc.		
(b) Purchase Money Mortgages:		
11.80% Series A, due September 30, 2015	**74.9**	74.9
10.30% Series B, due September 30, 2016	**200.0**	200.0
(c) Debentures and Medium Term Note Debentures:		
9.75% Series D, due December 17, 2006	**20.0**	20.0
10.75% Series E, due June 8, 2009	**59.9**	59.9
6.20% Series 9, due June 2, 2008	**188.0**	188.0
6.95% Series 11, due September 21, 2029	**150.0**	150.0
6.50% Series 12, due July 20, 2005	**200.0**	200.0
6.50% Series 13, due October 16, 2007	**100.0**	100.0
6.15% Series 16, due July 31, 2006	**100.0**	100.0
Floating Rate Series 17, interest rate of 2.93% (2003–3.02%) due September 26, 2005	**150.0**	150.0
6.50% Series 18, due May 1, 2034	**150.0**	—
Various series, weighted average interest rate of 9.63% (2002–9.63%) due in 2005	**45.0**	45.0
Obligations under capital leases, at 6.23% (2003–6.20%)	**10.8**	11.7
	1,448.6	1,299.5
Terasen Gas (Vancouver Island) Inc.		
(d) Syndicated credit facility at short-term floating rates, weighted average interest rate of 3.35% (2003–3.51%) with annual repayments of $5.4 million in 2005 and maturities of $176.5 million in 2006 and $33.0 million in 2009	**214.9**	220.4
Terasen Pipelines (Trans Mountain) Inc.		
(e) Debentures:		
10.75% Series B, due November 22, 2004	**—**	30.0
11.50% Series C, due June 20, 2010	**35.0**	35.0
	35.0	65.0
Terasen Pipelines (Corridor) Inc.		
(f) Commercial Paper at short-term floating rates, weighted average interest rate of 2.51% (2003–2.69%)	**446.0**	464.0
Other long-term debt	**13.8**	4.0
Total long-term debt	**2,583.3**	2,352.9
Less: current portion of long-term debt	**416.7**	51.8
	$ 2,166.6	$ 2,301.1

Terasen Inc. Medium Term Note Debentures:
The Company's Medium Term Note Debentures are unsecured obligations but are subject to the restrictions of the Trust Indenture dated November 21, 2001.

Terasen Gas Inc. Purchase Money Mortgages:
The Series A and Series B Purchase Money Mortgages are secured equally and rateably by a first fixed and specific mortgage and charge on Terasen Gas' Coastal Division assets, and are subject to the restrictions of the Trust Indenture dated December 3, 1990. The aggregate principal amount of Purchase Money Mortgages that may be issued under the Trust Indenture is limited to $425 million.

Terasen Gas Inc. Debentures and Medium Term Note Debentures:
Terasen Gas' debentures are unsecured obligations but are subject to the restrictions of the Trust Indenture dated November 1, 1977, as amended and supplemented.

Terasen Gas (Vancouver Island) Inc. Bank Syndicate:
The credit facility from the syndicate of banks is secured by a first floating charge over all of the assets of TGVI, assignment of certain material contracts, and assignment of royalty revenue and interruptible incentive payments.

Terasen Pipelines (Trans Mountain) Inc. Debentures:
The Trans Mountain debentures are unsecured obligations but are subject to the restrictions of the Trust Indenture dated February 18, 1987, as amended and supplemented.

Terasen Pipelines (Corridor) Inc. Commercial Paper:
The commercial paper program to finance the Corridor pipeline is supported by a syndicated bank credit facility that is committed until November 21, 2006.

The Company's Series 1 and Series 3 Medium Term Note Debentures, Terasen Gas' Series B Purchase Money Mortgages, Series E Debentures, and Series 11, Series 13, Series 16 and Series 18 Medium Term Note Debentures, and Trans Mountain's Series C Debentures are redeemable in whole or in part at the option of the Company at a price equal to the greater of the Canada Yield Price, as defined in the applicable Trust Indenture, and the principal amount of the debt to be redeemed, plus accrued and unpaid interest to the date specified for redemption. The Canada Yield Price is calculated as an amount that provides a yield slightly above the yield on an equivalent maturity Government of Canada bond.

Required principal repayments over the next five years are as follows:

2005	$	416.7
2006		834.4
2007		102.5
2008		390.5
2009		95.5

Required principal repayments in 2006 include $446.0 million in repayments with respect to Corridor which has been refinanced subsequent to year end as described in Note 19.

10. Other Long-Term Liabilities and Deferred Credits

		2004		2003
Pension and other post-employment benefit liabilities	$	**30.8**	$	20.5
Deferred gains for sale of natural gas distribution assets		**60.3**		30.2
Deferred payment		**33.9**		31.9
Other deferred credits/liabilities		**15.7**		17.2
	$	**140.7**	$	99.8

The deferred gains on sale of natural gas distribution assets occurred upon the sale and leaseback of pipeline assets to certain municipalities in 2001, 2002 and 2004. The pre-tax gains of $66.5 million on combined cash proceeds of $135.9 million are being amortized over the 17-year terms of the operating leases that commenced at the time of the sale transactions. These operating lease commitments are included in the table in Note 17.

The deferred payment resulted from the Company's acquisition of TGVI effective January 1, 2002. The deferred payment has a face value of $52.0 million but was discounted at January 1, 2002 to a present value of $28.2 million. The payment is due on December 31, 2011 or sooner if TGVI realizes revenues from transportation revenue contracts to serve power-generating plants which may be constructed in TGVI's service area. If any part of the deferred payment is paid prior to December 31, 2011, the difference between the payment and the carrying value of the debt will be treated as contingent consideration for the acquisition of TGVI and will be added to the cost of the purchase at that time.

Other deferred credits/liabilities includes amounts resulting from the Company's acquisition of TGVI effective January 1, 2002.

11. Capital Securities and Share Capital

Authorized Share Capital

The Company is authorized to issue 750,000,000 common shares, 100,000,000 first preference shares and 100,000,000 second preference shares, all without par value.

Capital Securities

On April 19, 2000, the Company issued $125.0 million of 8.0% Capital Securities with a term to maturity of 40 years for gross proceeds of $123.7 million. The Company may elect to defer payments on these securities and settle such deferred payments in either cash or common shares, and has the option to settle principal at maturity through the issuance of common shares. Accordingly, the capital securities have been classified as equity. The securities are exchangeable at the option of the holder on or after April 19, 2010 for common shares of the Company at 90% of the market price, subject to the right of the Company to redeem the securities for cash. Distributions on these securities, net of related income taxes, are deducted from net earnings for the purposes of calculating earnings applicable to common shares.

Stock Split

On June 14, 2004 the Company carried out a two-for-one stock split effected by paying a stock dividend of one additional common share for each common share held as of June 7, 2004.

All equity-based benefit plans have been amended to reflect the additional shares or options resulting from the stock split. All share and per share data has been amended for comparative and current periods to reflect the stock split.

Common Shares

Changes in the issued and outstanding common shares are as follows:

	2004		2003	
	Number	Amount	Number	Amount
Outstanding, beginning of year	**113,338,942**	**$ 868.7**	112,548,010	$ 858.6
Issued under: Share option plan	**1,009,761**	**14.5**	781,802	9.9
Employee share purchase plan	**6,962**	**0.2**	9,130	0.2
	114,355,665	**$ 883.4**	113,338,942	$ 868.7
Less common shares held by Trans Mountain	**9,184,188**		9,184,188	
Outstanding, end of year	**105,171,477**		104,154,754	

As at December 31, 2004, Trans Mountain owned 8.0% (2003–8.1%) of the common shares of Terasen Inc. The cost of these shares is shown as a deduction from shareholders' equity.

Reserved for Issue

At December 31, 2004 the number of common shares reserved for issue to meet rights outstanding is as follows:

Under share option plan	5,166,617
Under dividend reinvestment and share purchase plan	4,125,152
Under payroll deduction employee share purchase plan	808,994
	10,100,763

Earnings Per Share

Earnings per share are based on the weighted average number of common shares outstanding during the year. Diluted earnings per share are based on the weighted average number of common shares and dilutive stock options outstanding at the beginning of or granted during the year. The Company's performance based share options are considered to be contingently issuable shares and have been included in the treasury stock method calculation only if all performance criteria of the options have been satisfied. The possible exchange of the $125.0 million Capital Securities into common shares has not been included in the treasury stock method calculation since similar obligations in the past have been paid wholly in cash.

	2004		2003	
	Weighted average shares	Earnings	Weighted average shares	Earnings
Earnings applicable to common shares		**$ 149.8**		$ 132.7
Weighted average common shares	**104.7**		103.8	
Add: weighted average number of shares that would be issued under treasury stock method	**1.0**		1.0	
	105.7	**$ 149.8**	104.8	$ 132.7
Earnings per share		**$ 1.43**		$ 1.28
Diluted earnings per share		**$ 1.42**		$ 1.27

Shareholder Rights Plan

The Company established a Shareholder Rights Plan in 2003 that is designed to encourage the fair treatment of shareholders in connection with any takeover offer for the Company. Rights issued under the plan become exercisable when a person or party acquires or announces the intention to acquire 20% or more of the Company's outstanding common shares without complying with certain provisions set out in the plan or without approval of the Board of Directors of the Company. Each common share outstanding is entitled to one right, which entitles the rights holder, other than the acquiring person or party, the right to purchase common shares of the Company at 50% of the then market price.

12. Share Option Plan and Stock-Based Compensation

Share Option Plan

The Company has a Share Option Plan whereby officers and certain key employees may be granted options to purchase a maximum of 12,600,000 unissued common shares with terms up to ten years. There are two categories of options which have been issued under the Share Option Plan, Regular Share Options and Performance Based Share Options. The option exercise price is the closing sale price of the common shares on the Toronto Stock Exchange on the trading day prior to the date the option is granted.

Regular Share Options

Since 2000, the Company has granted options with eight-year terms which are exercisable on a cumulative basis and vest at one-third per year on the anniversary of the option grant date. Prior to 2000, the Company granted options with ten-year terms which are exercisable on a cumulative basis at 20% per year.

Regular Share Options Outstanding

	2004		2003	
	Shares under option	Weighted average exercise price	Shares under option	Weighted average exercise price
Outstanding, beginning of year	**1,118,822**	**$ 14.31**	1,518,792	$ 13.68
Options granted during the year	**24,800**	**23.93**	127,144	14.28
Options exercised	**(537,716)**	**13.39**	(497,716)	12.21
Options forfeited and expired	**(40,038)**	**17.46**	(29,398)	16.98
Outstanding, end of year	**565,868**	**$ 15.40**	1,118,822	$ 14.31
Options exercisable, end of year	**348,857**	**$ 13.25**	710,354	$ 12.28

	Options outstanding			Options exercisable	
Exercise price range	Shares under option	Weighted average exercise price	Weighted average remaining contractual life	Number exercisable at year-end	Weighted average exercise price
$6.94 – $13.33	180,780	$ 11.07	2.1	180,780	$ 11.07
$14.13 – $15.50	130,648	14.71	3.6	130,648	14.71
$17.56 – $24.00	254,440	18.82	5.6	37,429	18.68
	565,868	$ 15.40	4.0	348,857	$ 13.25

During 2004 the Company identified a number of regular share options that had been granted in 1994 and 1995 that had not been reflected in the outstanding balances upon the conversion of share option records to the external transfer agent in 1997. These 151,316 share options with a weighted average exercise price of $7.05 have been included in the continuity table above as an adjustment to the January 1, 2003 balance previously reported.

Performance-Based Share Options

The Company has granted performance-based share options with eight-year terms. The options vest at one-third per year on the anniversary of the option grant dates, subject to the market price of the Company's common shares reaching 125% of the option's exercise price for at least 10 out of 15 consecutive trading days within four years of the option grant date. If the market price requirement is not attained within four years of grant date, the participant is still eligible to exercise two-thirds of the granted options if the common share price reaches 125% of the option's exercise price for at least 10 out of 15 consecutive trading days during the subsequent four years.

Performance-Based Share Options Outstanding

	2004		2003	
	Shares under option	Weighted average exercise price	Shares under option	Weighted average exercise price
Outstanding, beginning of year	**2,304,398**	**$ 17.08**	1,892,184	$ 15.53
Options granted during the year	**716,600**	**23.88**	744,200	19.82
Options exercised	**(472,045)**	**15.53**	(284,086)	13.57
Options forfeited and expired	**(209,334)**	**19.68**	(47,900)	19.26
Outstanding, end of year	**2,339,619**	**$ 19.24**	2,304,398	$ 17.08
Options exercisable, end of year	**1,020,508**	**$ 16.27**	909,598	$ 12.79

	Options outstanding			Options exercisable	
Exercise price range	Shares under option	Weighted average exercise price	Weighted average remaining contractual life	Number exercisable at year-end	Weighted average exercise price
$11.25–$13.63	264,950	$ 12.77	2.8	264,950	$ 12.77
$15.50–$17.56	795,134	16.97	4.8	567,534	16.75
$19.60–$23.88	1,279,535	21.99	6.6	188,024	19.73
	2,339,619	$ 19.24	5.6	1,020,508	$ 16.27

Stock-Based Compensation

In 2004, 741,400 stock options were granted (2003–871,344) at an average exercise price of $23.88 (2003–$19.01) under the Company's Share Option Plan. The Company has applied the fair value based method of accounting for stock options granted after January 1, 2003. Reported earnings for 2004 include a compensation charge of $1.2 million (2003–$0.6 million) representing the fair value of options granted in 2003 and 2004 amortized over their respective vesting periods, with a corresponding increase to contributed surplus. Had the Company used the fair value based method to account for stock options granted during 2002, pro forma earnings and earnings per share would have been as follows:

		2004	2003
Net earnings (in millions)	As reported	**$ 156.4**	$ 139.4
	Pro forma	**$ 155.2**	$ 138.2
Earnings applicable to common shares (in millions)	As reported	**$ 149.8**	$ 132.7
	Pro forma	**$ 148.6**	$ 131.5
Basic earnings per common share	As reported	**$ 1.43**	$ 1.28
	Pro forma	**$ 1.42**	$ 1.27
Diluted earnings per common share	As reported	**$ 1.42**	$ 1.27
	Pro forma	**$ 1.41**	$ 1.26

A Black-Scholes model was used to calculate stock option fair values. The weighted average fair value of options granted in 2004 was $2.40 (2003 – $2.77). Significant assumptions in valuing the options are as follows:

	2004		2003	
	Regular Options	Performance Based	Regular Options	Performance Based
Interest rate	**3.5 – 3.7%**	**3.5%**	3.8 – 4.2%	4.3 – 4.4%
Expected volatility	**15.1 – 15.4%**	**15.4%**	16.8 – 17.8%	16.2 – 17.8%
Expected life	**5 years**	**6 years**	5 years	6 years

Deferred Share Units

The Company has issued Deferred Share Units ("DSU's") to certain senior employees and directors as compensation. At December 31, 2004, there were 52,859 (2003 – 22,104) DSU's outstanding, which had a fair value and carrying value of $1.5 million (2003 – $0.5 million). The liability is included in other long-term liabilities and deferred credits.

13. Employee Benefit Plans

The Company is a sponsor of pension plans for eligible employees. The plans include registered defined benefit pension plans, supplemental unfunded arrangements, which provide pension benefits in excess of statutory limits, and defined contributory plans. The Company also provides post-employment benefits other than pensions for retired employees. The following is a summary of each type of plan:

Defined Benefit Plans

Retirement benefits under the defined benefit plans are based on employees' years of credited service and remuneration. Company contributions to the plan are based upon independent actuarial valuations. The most recent actuarial valuations of the defined benefit pension plans for funding purposes were at December 31, 2002 and December 31, 2001 and the date of the next required valuations are December 31, 2005 and December 31, 2004. The December 31, 2004 valuation will not be completed until the second quarter of 2005. The expected weighted average remaining service life of employees covered by the defined benefit pension plans is 11.8 years (2003 – 11.8 years).

Defined Contribution Plan

Effective in 2000 for Terasen Gas and 2003 for petroleum transportation operations, all new non-union employees become members of defined contribution pension plans. Company contributions to the plan are based upon employee age and pensionable earnings for employees of the natural gas distribution operations and pensionable earnings for employees of the petroleum transportation operation.

Supplemental Plans

Certain employees are eligible to receive supplemental benefits under both the defined benefit and defined contribution plans. The supplemental plans provide pension benefits in excess of statutory limits. The supplemental plans are unfunded and are secured by letters of credit.

Other Post-Employment Benefits

The Company provides retired employees with other post-employment benefits that include, depending on circumstances, supplemental health, dental and life insurance coverage. Post-employment benefits are unfunded and annual expense is recorded on an accrual basis based on independent actuarial determinations, considering among other factors, health care cost escalation. The most recent actuarial valuations were completed as at December 31, 2002. The expected weighted average remaining service life of employees covered by these benefit plans is 9.9 years (2003 – 9.9 years).

The Company measures its accrued benefit obligations and the fair value of plan assets for accounting purposes as at December 31 each year. The financial positions of the employee defined benefit pension plans and other benefit plans are presented in aggregate in the tables below:

	Defined benefit pension plans		Other benefit plans	
	2004	2003	**2004**	2003
Plan assets				
Fair value, beginning of year	**$ 255.3**	$ 221.2	**$ —**	$ —
Acquisition of Express System	**—**	1.9	**—**	—
Actual return on plan assets	**26.7**	31.1	**—**	—
Employers' contributions	**5.5**	10.2	**1.5**	1.2
Employees' contributions	**2.9**	3.0	**—**	—
Benefits and settlements paid	**(15.2)**	(11.4)	**(1.4)**	(1.1)
Other	**(0.7)**	(0.7)	**(0.1)**	(0.1)
Fair value, end of year	**274.5**	255.3	**—**	—
Accrued benefit obligation				
Obligation, beginning of year	**276.7**	250.8	**61.0**	49.9
Acquisition of Express System	**—**	1.4	**—**	0.6
Current service cost	**8.1**	7.9	**1.3**	1.5
Interest cost	**17.2**	16.6	**3.9**	3.4
Employees' contributions	**2.9**	3.0	**—**	—
Benefits and settlements paid	**(15.2)**	(11.4)	**(1.4)**	(1.1)
Change in discount rate	**7.8**	8.3	**2.5**	2.4
Actuarial (gain) loss	**—**	(1.4)	**—**	11.5
Past service cost and other	**0.5**	1.5	**—**	(7.2)
Balance, end of year	**298.0**	276.7	**67.3**	61.0
Funded status – plan deficit	**(23.5)**	(21.4)	**(67.3)**	(61.0)
Unamortized transitional obligation (benefit)	**(27.2)**	(31.0)	**6.2**	7.8
Unamortized actuarial loss	**43.2**	47.8	**32.0**	32.1
Unamortized past service costs	**9.0**	8.7	**(3.2)**	(3.5)
Accrued benefit asset (liability)	**$ 1.5**	$ 4.1	**$ (32.3)**	$ (24.6)

The net accrued benefit liability is included in other long-term liabilities and deferred credits (Note 10).

Included in the accrued benefit obligation and fair value of the plan assets at year-end are the following amounts in respect of plans with accrued benefit obligations in excess of fair value of assets:

	Pension benefit plans		Other benefit plans	
	2004	2003	**2004**	2003
Accrued benefit obligations:				
Unfunded plans	**$ 28.0**	$ 25.3	**$ 67.3**	$ 61.0
Funded plans	**156.5**	142.7	**—**	—
	184.5	168.0	**67.3**	61.0
Fair value of plan assets	**151.9**	135.1	**—**	—
Funded status deficit	**$ (32.6)**	$ (32.9)	**$ (67.3)**	$ (61.0)

The accrued benefit obligations for unfunded pension benefit plans are secured by letters of credit.

The net benefit plan expense is as follows:

	Pension benefit plans		Other benefit plans	
	2004	2003	**2004**	2003
Current service cost	**$ 8.1**	$ 7.9	**$ 1.3**	$ 1.5
Interest cost on projected benefit obligations	**17.2**	16.6	**3.9**	3.4
Actual return on plan assets	**(26.7)**	(31.1)	**—**	—
Net actuarial losses	**7.8**	6.9	**2.5**	14.0
Past service costs	**0.5**	0.3	**—**	(8.6)
Net benefit plan expense before adjustments	**6.9**	0.6	**7.7**	10.3
Adjustments to recognize the long-term nature of employee future benefit costs:				
Difference between actual and expected return on plan assets	**7.7**	13.0	**—**	—
Difference between actual and recognized actuarial gains (losses) in year	**(5.2)**	(6.1)	**0.1**	(13.0)
Difference between actual and recognized past service costs in year	**0.1**	0.3	**(0.3)**	8.7
Amortization of transitional obligation (benefit)	**(3.4)**	(3.4)	**1.6**	2.7
Other	**1.5**	0.6	**—**	—
Net benefit plan expense	**$ 7.6**	$ 5.0	**$ 9.1**	$ 8.7
Defined contribution plan expense	**$ 2.3**	$ 1.6		
	$ 9.9	$ 6.6		

Benefit Plan Assets

The weighted-average asset allocation by asset category of the Company's funded defined benefit pension plans is as follows:

	2004	2003
Equity securities	**55%**	58%
Fixed income securities	**40%**	36%
Other assets	**5%**	6%
Total assets	**100%**	100%

The investment policy for benefit plan assets is to optimize the risk-return using a portfolio of various asset classes. The Company's primary investment objectives are to secure registered pension plans, and maximize investment returns in a cost-effective manner while not compromising the security of the respective plans. The pension plans utilize external investment managers to manage the investment policy. Assets in the plan are held in trust by independent third parties.

The pension plans do not directly hold any shares of the Company.

Significant Assumptions

The discount rate assumption used in determining pension and post-retirement benefit obligations and net benefit expense reflects the market yields, as of the measurement date, on high-quality debt instruments. The expected rate of return on plan assets assumption is reviewed annually by management, in conjunction with actuaries. The assumption is based on the expected returns for the various asset classes, weighted by the portfolio allocation.

The weighted average significant actuarial assumptions used to determine the accrued benefit obligation and the benefit plan expense are as follows:

	Pension benefit plans		Other benefit plans	
	2004	2003	**2004**	2003
Accrued benefit obligation				
Discount rate at December 31, based on AA Corporate bonds	**6.00%**	6.25%	**6.00%**	6.25%
Rate of compensation increase	**3.50%**	3.39%	**—**	—
Net benefit plan expense				
Discount rate at January 1, based on AA Corporate bonds	**6.25%**	6.25%	**6.25%**	6.25%
Expected rate of return on plan assets	**7.50%**	7.50%	**—**	—

The assumed health-care cost trend rates for other post-employment benefit plans are as follows:

	2004	2003
Extended health benefits		
Initial health care cost trend rate	**9.0%**	10.0%
Annual rate of decline in trend rate	**1.0%**	1.0%
Ultimate health care cost trend rate	**5.0%**	5.0%
Year that the rate reaches the ultimate trend rate	**2008**	2008
Medical Services Plan Benefits Premium trend rate	**4.0%**	4.0%

A one percentage-point change in assumed health-care cost trend rates would have the following effects:

2004	One percentage-point increase	One percentage-point decrease
Effect on total of the service costs and interest cost components of the benefit plan expense	**$ 1.1**	**$ (1.0)**
Effect on accrued benefit obligation	**13.1**	**(10.8)**

Cash Flows

Total cash contributions for employee benefit plans consist of:

	Pension benefit plans	
	2004	2003
Funded plans	**$ 4.3**	$ 9.4
Beneficiaries of unfunded plans	**2.7**	2.0
Defined contribution plans	**2.3**	1.6
Total	**$ 9.3**	$ 13.0

The contributions for 2005 are anticipated to be approximately the same as 2004 for both the defined pension benefit plans and other benefit plans.

Benefit Changes

Effective January 1, 2004, the Company modified its post-employment benefit program for non-union active employees in order to provide future retirees with more choice of coverage and to reduce the Company's exposure to future health and group life cost increases. The new plan is predominantly a defined contribution plan incorporating a Company-paid health spending account, a security health plan and life insurance. Provincial medical services plan premiums will now be paid by the retiree.

All plan members who have retired on or before December 31, 2004 receive benefits under the plans that were in effect when they retired, which includes the payment of provincial medical services plan premiums by the Company. Employees electing to retire during 2005 will have a choice between the new and old plan, and employees retiring after December 31, 2005 will participate in the new plan.

These assumptions, including the post-employment benefit plan changes, were included in the calculation of the accrued benefit obligation at December 31, 2003 and 2004.

14. Financing Costs

		2004		2003
Interest and expense on long-term debt	$	141.6	$	155.6
Interest on short-term debt		26.1		29.0
Interest capitalized		(1.1)		(8.6)
	$	166.6	$	176.0

15. Income Taxes

Provision For Income Taxes

		2004		2003
Current income taxes	$	69.7	$	49.6
Future income taxes		(0.5)		9.4
	$	69.2	$	59.0

Variation in Effective Income Tax Rate

Consolidated income taxes vary from the amount that would be computed by applying the Canadian and United States Federal, British Columbia and Alberta combined statutory income tax rate of 34.52% (2003–36.47%) to earnings before income taxes as shown in the following table:

		2004		2003
Earnings before income taxes	$	225.6	$	198.4
Combined statutory income tax rate		34.52%		36.47%
Combined income taxes at statutory rate	$	77.9	$	72.4
Increase (decrease) in income taxes resulting from:				
Capital cost allowance and other deductions claimed for income tax purposes over amounts recorded for accounting purposes		(14.7)		(19.4)
Large Corporations Tax in excess of surtax		6.6		7.8
Non-deductible expenses and non-taxable income		5.5		7.5
Benefit of tax rate changes on losses		(0.4)		(3.3)
Equity income not subject to tax		(3.3)		(2.6)
Other		(2.4)		(3.4)
Actual consolidated income taxes	$	69.2	$	59.0
Effective income tax rate		30.67%		29.74%

Future Income Taxes

The net future income tax liability of the Company of $68.7 million (2003–$67.5 million) relates primarily to the tax effect of temporary differences on non-regulated property, plant and equipment balances.

As a result of the Company accounting for income taxes following the taxes payable method for its natural gas distribution and petroleum transportation regulated operations, the Company has not recognized net future income tax liabilities amounting to $278.7 million at December 31, 2004 (2003–$263.5 million) and has not recognized a future income tax expense of $15.2 million for the year ended December 31, 2004 (2003–$17.9 million), all of which were calculated using the asset and liability method.

16. Financial Instruments

Fair Value Estimates

The carrying values of cash and short-term investments, accounts receivable, short-term notes and accounts payable and accrued liabilities approximate their fair values due to the relatively short period to maturity of the instruments.

The fair value of the Company's investment in the Express System is estimated to approximate its carrying value.

The fair value of the Company's long-term debt, calculated by discounting the future cash flow of each debt issue at the estimated yield to maturity for the same or similar issues at December 31, 2004, or by using available quoted market prices, is estimated at $2,818.2 million (2003 – $2,565.3 million). The majority of the Company's long-term debt relates to regulated operations which enables the Company to recover the existing financing charges through rates or tolls.

Fair value estimates are made at a specific point in time, based on relevant market information and information about the financial instrument. These estimates cannot be determined with precision as they are subjective in nature and involve uncertainties and matters of judgment.

Derivative Instruments

The Company uses derivative instruments to hedge its exposures to fluctuations in natural gas prices, interest rates and foreign currency exchange rates.

Asset (Liability) December 31 (in millions)	Number of swaps	Term to maturity (years)	**2004** Carrying Value	Fair Value	2003 Carrying Value	Fair Value
Interest Rate Swaps						
Terasen Inc.	2	1 – 4	**$ 0.4**	**$ 5.4**	$ 0.4	$ 5.3
TGVI	4	1 – 4	**(0.5)**	**(3.2)**	(1.5)	(4.8)
Natural Gas Commodity Swaps						
TGI and TGVI	139	Up to 2	**1.9**	**(8.3)**	(7.8)	6.3
Clean Energy	7	Up to 5	**6.5**	**6.5**	—	—
Foreign Currency Swaps						
Terasen Inc.	2	1	**(0.6)**	**(0.6)**	0.8	0.8
TGI	—	—	**—**	**—**	—	(0.9)

The natural gas derivatives fair value reflects only the value of the natural gas derivatives and not the offsetting change in value of the underlying future purchases of natural gas. These fair values reflect the estimated amounts the Company would receive or pay to terminate the contracts at the stated dates.

Clean Energy, an entity in which the Company holds a 45% interest, has purchased gas forward contract positions to offset future commodity supply contracts. Since these contracts have not been specifically designated as hedges, these positions are marked-to-market at each balance sheet date and gains or losses are reported in the statement of earnings as cost of revenues from other activities. During the year ended December 31, 2004 the Company has included in earnings an amount of $3.3 million (2003 – nil) net of tax and estimated selling expenses pertaining to the Company's proportionate share of Clean Energy's gas forward contracts.

The derivatives entered into by TGVI relate to regulated operations and any resulting gains or losses are recorded in a deferral account (RDDA), subject to regulatory approval, and passed through to customers in future rates.

As at December 31, 2004, the Company had two U.S. dollar foreign currency derivatives outstanding which are being used to mitigate foreign currency exposure in the investment in the Express System and Terasen International Inc. The change in fair value of the derivative to mitigate foreign currency exposure in the Express System of $0.6 million loss (2003 – $0.8 million income) has been included in the earnings of the Express System.

The Company is exposed to credit risk in the event of non-performance by counterparties to derivative instruments. Because it deals with high credit quality institutions in accordance with established credit approval practices, the Company does not expect any counterparties to fail to meet their obligations.

17. Commitments & Contingencies

The Company's subsidiaries and proportionately consolidated entities have entered into operating leases for certain building space and natural gas distribution assets. In addition, Terasen Gas and TGVI have entered into gas purchase contracts and Trans Mountain has entered into a contract to purchase power at fixed rates that expires in 2005, which cumulatively represent future purchase obligations.

The following table sets forth the Company's operating lease and gas and power purchase obligations due in the years indicated:

	Operating leases	Purchase obligations	Total
2005	$ 24.1	$ 766.8	$ 790.9
2006	23.0	324.5	347.5
2007	21.3	70.6	91.9
2008	21.4	20.1	41.5
2009	19.8	15.9	35.7
2010 and later	143.2	—	143.2
	$ 252.8	$ 1,197.9	$ 1,450.7

Gas purchase contract commitments are based on market prices that vary with gas commodity indices. The amounts disclosed reflect index prices that were in effect at December 31, 2004.

On January 4, 2005 Terasen Gas terminated an operating lease for a certain building and paid $49.4 million to acquire the related building. Accordingly, payments related to this operating lease are not included in the above table. Effective January 4, 2005 the building is included in property, plant and equipment and has been included in Terasen Gas' rate base revenue requirement for 2005.

In prior years, TGVI received non-interest bearing, repayable loans from the Federal and Provincial governments of $50 million and $25 million respectively, in connection with the construction and operation of the Vancouver Island natural gas pipeline. The government loans are repayable in any fiscal year after 2002 and prior to 2012 under certain circumstances and subject to the ability of TGVI to obtain non-government subordinated debt financing on reasonable commercial terms. As approved by the BCUC, these loans have been recorded as a government grant and have reduced the amounts reported for property, plant and equipment. The Company anticipates that all of the repayment criteria may be met in 2005 and, if met, will result in an estimated repayment of $5.8 million of these loans in 2005. As the loans are repaid and replaced with non-governmental loans, plant and equipment and long-term debt will increase in accordance with the approved capital structure, as will the rate base used in determining rates. The amounts are not included in the obligations in the table above as the amounts and timing of repayments is dependent upon the approved RDDA recovery each year and the ability to replace the loans with non-government subordinated debt financing on reasonable commercial terms.

A number of claims and lawsuits seeking damages and other relief are pending against the Company. Management is of the opinion, based upon information presently available, that it is unlikely that any liability, to the extent not provided for through insurance or otherwise, would be material in relation to the Company's consolidated financial statements.

18. Guarantees

The Company has, for a fee, arranged for the issuance of a letter of credit in the amount of US$13.4 million on behalf of co-investors in the Express System to fund the Debt Service Reserve Account required under the Express System's trust indenture. The letter of credit is subject to annual renewal. If the letter of credit is drawn upon, the Company will have recourse to the co-investors, major Canadian pension funds.

The Company has, for a fee, provided indemnities with respect to performance bonds issued on behalf of Clean Energy in the amount of US$7.2 million. These performance bonds secure construction projects undertaken by Clean Energy, and have expiry dates of one year from the date of issue.

19. Subsequent Event

On February 1, 2005, Corridor issued $150 million principal amount of unsecured debentures, Series A, maturing February 2, 2010 at an interest rate of 4.24%, and $150 million principal amount of unsecured debentures, Series B, maturing February 2, 2015 at an interest rate of 5.033%. The proceeds were used to repay a portion of Corridor's outstanding commercial paper. Concurrently with this financing, Corridor replaced its credit facility due November 21, 2006 with a new credit facility with annual renewal provisions. Corridor's commercial paper will accordingly be classified as short-term debt prospectively.

Unaudited
Dollar amounts in millions

Years ended December 31	2004	2003	2002	2001	2000	1999
Statements of earnings						
Operating revenue	**$ 1,957.0**	$ 1,876.6	$ 1,707.2	$ 1,666.3	$ 1,305.6	$ 1,040.6
Operating expenses	**1,579.8**	1,510.2	1,370.7	1,371.1	1,049.0	784.7
Operating income	**377.2**	366.4	336.5	295.2	256.6	255.9
Other expenses	**166.6**	176.0	160.8	148.3	131.0	121.6
Share of (earnings) of Express System	**(15.0)**	(8.0)	—	—	—	—
Income taxes	**69.2**	59.0	63.2	55.9	8.9	48.4
Non-controlling interest	**—**	—	—	—	4.0	4.7
Net earnings	**156.4**	139.4	112.5	91.0	112.7	81.2
Capital securities distributions	**6.6**	6.7	6.7	6.4	3.9	—
Earnings applicable to common shares	**$ 149.8**	$ 132.7	$ 105.8	$ 84.6	$ 108.8	$ 81.2
Assets						
Current assets	**$ 596.1**	$ 583.2	$ 482.9	$ 503.5	$ 631.2	$ 270.7
Property, plant and equipment (net)	**3,892.5**	3,882.4	3,779.2	3,079.9	2,727.6	2,185.1
Investment in Express System	**218.9**	204.6	—	—	—	—
Other assets	**263.1**	251.1	260.3	122.3	154.3	25.1
Total assets	**$ 4,970.6**	$ 4,921.3	$ 4,522.4	$ 3,705.7	$ 3,513.1	$ 2,480.9
Liabilities and Shareholders' Equity						
Current liabilities	**$ 1,098.5**	$ 1,025.4	$ 878.9	$ 857.7	$ 1,094.4	$ 712.4
Long-term debt	**2,166.6**	2,301.1	2,123.4	1,928.0	1,561.9	1,001.8
Other long-term liabilities and deferred credits	**140.7**	99.8	96.4	23.1	—	—
Other liabilities	**68.7**	67.5	58.1	56.8	47.3	140.4
Shareholders' equity	**1,496.1**	1,427.5	1,365.6	840.1	809.5	626.3
Total liabilities and shareholders' equity	**$ 4,970.6**	$ 4,921.3	$ 4,522.4	$ 3,705.7	$ 3,513.1	$ 2,480.9
Cash Flow Data						
Operating cash flow	**$ 342.0**	$ 269.8	$ 318.1	$ 59.8	$ 179.3	$ 124.1
Capital expenditures	**$ 154.4**	$ 222.9	$ 395.7	$ 469.8	$ 620.6	$ 163.6

Unaudited
Dollar amounts in millions

Years ended December 31	2004	2003	2002	2001	2000	1999
Natural Gas Distribution Operations						
Revenues						
Residential	$ **836.8**	$ 828.8	$ 779.6	$ 813.6	$ 627.8	$ 493.2
Commercial	**411.5**	409.6	382.3	442.2	336.3	262.2
Small industrial	**70.4**	77.6	76.7	73.6	52.3	26.7
Large industrial and other	**30.6**	33.7	27.4	6.8	7.7	8.8
Total natural gas sales revenue	**1,349.3**	1,349.7	1,266.0	1,336.2	1,024.1	790.9
Transportation	**95.1**	90.9	83.8	56.1	41.0	38.4
Other	**49.7**	57.3	52.9	28.0	20.3	15.4
Total natural gas revenue	$ **1,494.1**	$ 1,497.9	$ 1,402.7	$ 1,420.3	$ 1,085.4	$ 844.7
Natural gas volumes *(billion cubic feet)*						
Sales volumes	**111.2**	116.7	126.0	110.8	124.0	121.8
Transportation volumes	**65.8**	67.1	61.3	53.9	56.3	57.6
Throughput under fixed-price contracts	**16.0**	11.7	22.6	63.9	57.9	38.0
Total natural gas volumes	**193.0**	195.5	209.9	228.6	238.2	217.4
Customers at year end	**875,166**	859,183	850,699	767,855	762,878	755,383
Rate base–Terasen Gas Inc.	$ **2,310.1**	$ 2,280.6	$ 2,223.8	$ 2,249.8	$ 1,715.1	$ 1,637.4
Rate base–Terasen (Vancouver Island)	**459.3**	457.3	472.9	N/A	N/A	N/A
	$ **2,769.4**	$ 2,737.9	$ 2,696.7	$ 2,249.8	$ 1,715.1	$ 1,637.4
Petroleum Transportation Operations						
Revenues	$ **225.5**	$ 200.0	$ 136.0	$ 143.1	$ 132.5	$ 129.4
Transportation volumes *(bpd)*						
Trans Mountain						
Canadian mainline	**236,100**	216,100	201,200	209,300	204,600	207,500
U.S. mainline *(included in Canadian mainline)*	**91,700**	54,600	47,800	73,400	65,200	61,900
Express Sytem	**175,300**	171,200	N/A	N/A	N/A	N/A
Kilometres of pipelines						
Natural gas distribution operations	**44,168**	43,777	43,196	37,430	37,197	36,581
Petroleum transportation operations	**4,720**	4,720	1,477	1,477	1,477	1,477
Employees *(consolidated)*	**2,553**	2,082	2,051	1,782	1,966	1,869

Unaudited

Years ended December 31	2004	2003	2002	2001	2000	1999
Ratios						
Return on average common equity	**11.2%**	10.7%	11.7%	12.1%	12.0%	12.2%
Dividend payout ratio	**58%**	60%	57%	59%	43%	55%
Interest coverage ratio	**2.4**	2.1	2.1	2.0	2.2	2.1
Equity to total capital	**35%**	33%	34%	26%	29%	31%
Common shares outstanding–weighted average[1]	**104.7**	103.8	86.4	76.7	76.6	76.5
Data Per Common Share[1]						
Earnings before non-recurring items	**$ 1.43**	$ 1.31	$ 1.22	$ 1.10	$ 1.03	$ 0.97
Earnings after non-recurring items	**$ 1.43**	$ 1.28	$ 1.22	$ 1.10	$ 1.42	$ 1.06
Dividends	**$ 0.825**	$ 0.765	$ 0.705	$ 0.650	$ 0.613	$ 0.583
Operating cash flow	**$ 3.27**	$ 2.60	$ 3.68	$ 0.78	$ 2.34	$ 1.62
Common equity	**$ 13.04**	$ 12.51	$ 12.00	$ 9.32	$ 8.93	$ 8.18
Market price range–High	**$ 28.59**	$ 24.25	$ 21.25	$ 18.44	$ 16.75	$ 15.70
Market price range–Low	**$ 21.50**	$ 18.08	$ 16.28	$ 14.50	$ 10.75	$ 10.23
Market price range–Close	**$ 27.71**	$ 23.98	$ 19.08	$ 16.60	$ 16.68	$ 12.70

[1]All share and per share data has been restated to reflect the 2-for-1 share split, which took effect in June 2004.

Unaudited
In millions, except where stated otherwise[1]

	Three months ended				Year ended
2004	March	June	September	December	December
Revenues	**$ 648.2**	**$ 365.3**	**$ 327.1**	**$ 616.4**	**$ 1,957.0**
Net earnings	**$ 69.5**	**$ 19.6**	**$ 11.7**	**$ 55.6**	**$ 156.4**
Earnings applicable to common shares	**$ 67.9**	**$ 17.9**	**$ 10.1**	**$ 53.9**	**$ 149.8**
Data per common share[1]					
Basic earnings	**$ 0.65**	**$ 0.17**	**$ 0.10**	**$ 0.51**	**$ 1.43**
Diluted earnings	**$ 0.64**	**$ 0.17**	**$ 0.10**	**$ 0.51**	**$ 1.42**
Dividends paid	**$ 0.195**	**$ 0.210**	**$ 0.210**	**$ 0.210**	**$ 0.825**
Common share trading – TSX[1]					
High	**$ 25.00**	**$ 24.86**	**$ 25.05**	**$ 28.59**	**$ 28.59**
Low	**$ 22.18**	**$ 21.50**	**$ 23.07**	**$ 24.35**	**$ 21.50**
Close	**$ 24.41**	**$ 23.62**	**$ 24.61**	**$ 27.71**	**$ 27.71**
Volume	**12.7**	**9.5**	**6.6**	**5.4**	**34.2**
Common shares outstanding – weighted average[1]	**104.4**	**104.7**	**104.8**	**105.0**	**104.7**

2003					
Revenues	$ 556.0	$ 400.4	$ 304.5	$ 615.7	$ 1,876.6
Net earnings	$ 65.4	$ 16.2	$ 5.2	$ 52.6	$ 139.4
Earnings applicable to common shares	$ 63.7	$ 14.6	$ 3.5	$ 50.9	$ 132.7
Data per common share[1]					
Basic earnings	$ 0.62	$ 0.14	$ 0.03	$ 0.49	$ 1.28
Diluted earnings	$ 0.61	$ 0.14	$ 0.03	$ 0.48	$ 1.27
Dividends paid	$ 0.180	$ 0.195	$ 0.195	$ 0.195	$ 0.765
Common share trading – TSX[1]					
High	$ 20.00	$ 22.37	$ 22.47	$ 24.25	$ 24.25
Low	$ 18.08	$ 18.25	$ 20.88	$ 21.57	$ 18.08
Close	$ 18.48	$ 21.78	$ 21.75	$ 23.98	$ 23.98
Volume	9.2	12.4	11.4	8.2	41.2
Common shares outstanding – weighted average[1]	103.5	103.8	103.9	104.1	103.8

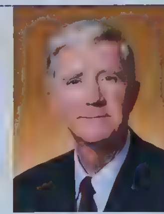
[1]*All share and per share data has been restated to reflect the 2-for-1 share split, which took effect in June 2004.*

Board of Directors


Mark L. Cullen


Randolph C. Aldridge
1, 2


Brian A. Canfield
1, 2


Thomas S. Chambers
1, 2


Pierre Choquette
1, 3


Ida J. Goodreau
3, 4


Eric P. Newell
1, 4


Michael W. O'Brien
1, 3


John M. Reid


James M. Stanford
3, 4


Dr. David W. Strangway
2, 3

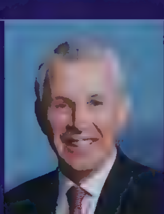

Douglas W. G. Whitehead
2, 4

Committees of the Board

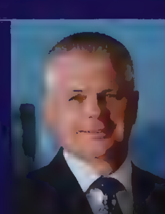
1 Audit Committee
2 Corporate Governance & Nominating Committee
3 Health, Environment & Safety Cor
4 Management Resources Committe

Terasen Inc. directors are also directors of Terasen Gas Inc. and Terasen Pipelines (Trans Mountain) Inc.

Executive Officers


John M. Reid


Richard T. Ballantyne


Gordon R. Barefoot


Brett T. Hodson


Randall L. Jespersen


Patrick D. Lloyd


Stephen M. G. Richards


Stephen J. Swaffield

Mark L. Cullen, of Vancouver, British Columbia, is Chairman of the Board of Terasen Inc. and former Vice Chairman of RBC Dominion Securities. During the past five years he has been a director of Bentall Corporation, British Columbia Ferry Corporation, Canfor Corporation, MacDonald Dettwiler & Associates Limited and Weldwood of Canada Limited. He is currently a director of Wajax Limited. He joined the Board of Terasen in 1998.

Randolph C. Aldridge, of San Antonio, Texas, is an energy industry consultant. He has held senior management positions with Koch Industries, including Chairman of Koch Pipelines Canada, President of Koch Canada, and President of Koch Oil Co., U.S. He serves on the Board of the Free Trade Alliance and is a member of the Texas A&M Chemical Engineering Advisory Council. He joined the Board of Terasen in 2005. **1, 2**

Brian A. Canfield, of Point Roberts, Washington, is Chairman of TELUS Corporation and former Chairman, President and CEO of BC Telecom. He serves on the boards of Suncor Energy Inc. and the Canadian Public Accountability Board. He joined the Board of Terasen in 1996. **1, 2**

Thomas S. Chambers, F.C.A. of Vancouver, British Columbia, is a corporate director and business advisor with Senior Partner Services Ltd. He serves on the boards of Norske Skog Canada Limited, Elephant and Castle Group Inc., Mill and Timber Group, the BC Cancer Foundation and the Victorian Order of Nurses. He joined the Board of Terasen in 2003. **1, 2**

Pierre Choquette, of Vancouver, British Columbia, is Chairman of the Board of Methanex Corporation. From 2003 to 2004 he was Chairman and CEO and from 1994 to 2003 he was President and CEO of Methanex. He previously held senior positions with NOVA Corporation and Polysar Ltd. He joined the Board of Terasen in 2003. **1, 3**

Ida J. Goodreau, of Vancouver, British Columbia, is President and CEO of the Vancouver Coastal Health Authority. She is also a director of Shell Canada Limited. She previously held senior executive positions with Norske Skog, Fletcher Challenge Canada Limited, Tasman Pulp and Paper, and Union Gas Ltd. She joined the Board of Terasen in 2002. **3, 4**

Eric P. Newell, O.C. of Edmonton, Alberta, is Chancellor of the University of Alberta. He is also Chairman of Careers: The Next Generation Foundation and is former Chairman and CEO of Syncrude Canada Ltd. He serves on the boards of Nexen Inc., Canfor Corporation, C.D. Howe Institute and the Alberta Energy Research Institute and is policy advisor to the Learning Partnership. He joined the Board of Terasen in 2004. **1, 4**

Michael W. O'Brien, of Canmore, Alberta, is a director of Suncor Energy Inc., PrimeWest Energy Inc., and Shaw Communications Inc. Prior to retiring in 2002, he was Executive V.P. and CFO of Suncor Energy Inc. He is also a member of the Board of Trustees for the Nature Conservancy of Canada. He joined the Board of Terasen in 2002. **1, 3**

John M. Reid, of Vancouver, British Columbia, is President and CEO of Terasen Inc. Before joining Terasen, he worked with Scott Paper Limited in senior financial positions and as President and CEO. He serves on the boards of Methanex Corporation, the Conference Board of Canada and the Board of Governors of the University of British Columbia. He is also a member of the Canadian Council of Chief Executives and the Business Council of B.C. He joined the Board of Terasen in 1997.

James M. Stanford, O.C. of Calgary, Alberta, is President of Stanford Resource Management Inc. and former President and CEO of Petro-Canada. He is Chair of the Canadian Foundation for Sustainable Development Technology, and serves on the boards of EnCana Corporation, NOVA Chemicals Corporation, Inco Limited, OMERS Resources, Iogen Corporation and OPTI Canada Inc. He joined the Board of Terasen in 2001. **3, 4**

Dr. David W. Strangway, of Vancouver, British Columbia, is President of Sea to Sky University. He served as President and CEO of the Canada Foundation for Innovation from 1998 to 2004 and as President of the University of British Columbia from 1985 to 1997. He has served on numerous scientific and academic committees. He joined the Board of Terasen in 1991. **2, 3**

Douglas W. G. Whitehead, of Vancouver, British Columbia, is President and CEO of Finning International Inc. Prior to joining Finning, he was President and CEO of Fletcher Challenge Canada Limited. He serves on the boards of Ballard Power Systems Inc., Belkorp Industries Inc., the Conference Board of Canada and the University of British Columbia. He is a member of the Canadian Council of Chief Executives. He joined the Board of Terasen in 2000. **2, 4**

John M. Reid, President and Chief Executive Officer, joined Terasen in 1995 as Executive Vice President, Finance and Chief Financial Officer. He has served as president and CEO since 1997. Please see the more detailed description above.

Richard T. Ballantyne was named President of Terasen Pipelines in 2002. He has worked with Terasen for 18 years through its predecessors Trans Mountain Pipe Line and BC Gas Utility Ltd. Rich is a board member of the Canadian Energy Pipeline Association, the Association of Oil Pipelines and the Pipeline Division of the American Petroleum Institute.

Gordon R. Barefoot was named Senior Vice President, Finance and Chief Financial Officer in 2004, having previously held the positions of Senior Vice President, Planning and Development and Senior Vice President, Multi Utility Services. Gord is Chairman of the Board of Vancouver Community College and has served on the Alberta Financial Review Commission and the British Columbia Fiscal Review Panel.

Brett T. Hodson was named President of Terasen Water and Utility Services in 2001, having held a number of positions in the areas of marketing, resource planning and market/business development at Terasen Gas. He has worked in the energy and utility industry for 14 years.

Randall L. Jespersen was appointed President of Terasen Gas in 2002, having previously held the positions of Senior Vice President, Energy Delivery Services and Senior Vice President, Gas Supply. He is past chair of the Western Energy Institute and is a board member of the Canadian Gas Association. Randy is a member of the United Way Community Campaign Cabinet for B.C.'s Lower Mainland.

Patrick D. Lloyd is Senior Vice President, Human Resources and Government Affairs. Since joining Terasen's predecessor Inland Natural Gas in 1980, he has held senior vice president roles in Operations, Gas Supply, Finance, IT, Government and Regulatory Affairs and Customer Service. Patrick has served as Chairman of the Canadian Gas Association, as a board member of the American Gas Association and on the executive committee of the International Gas Union.

Stephen M. G. Richards joined Terasen in 1988 and was appointed Senior Vice President, General Counsel and Corporate Secretary in 2005, overseeing the legal, governance and risk management affairs for the Terasen group of companies. He serves on a number of national and provincial professional and community boards.

Stephen J. Swaffield was appointed Senior Vice President, Corporate Development in 2004. Prior to joining the company, he was an investment banker with RBC Capital Markets where he assisted Terasen with the acquisition of Centra BC and the financing of the Express Pipeline.

Annual General Meeting
The Annual General Meeting of Shareholders will be held at 11:00 a.m. on Wednesday, May 4, 2005 at the Fairmont Waterfront Hotel in Vancouver, British Columbia.

Dividend Reinvestment and Share Purchase Plan
Registered holders of the Company's Common shares (except residents of the United States) may elect to reinvest their cash dividends in new Common shares. Participants in the Plan may also make optional cash payments of up to $20,000 per calendar year to purchase additional Common shares. Optional cash payments must be received by the Registrar and Transfer Agent by the last days of January, April, July and October to be reinvested on the following dividend payment date. There are no brokerage commissions payable on shares purchased pursuant to the Plan. For an information package on the Plan, or to register in the Plan, please contact Shareholder Relations.

Employee Share Purchase Plan
Terasen employees may contribute from 2% to 6% of their earnings through payroll deductions to purchase the Company's Common shares. Shares are purchased at 100% of the market price.

Common Share Distribution
Approximately 99.5% of the outstanding Common shares are owned by residents of Canada. The following table summarizes the distribution of shares at December 31, 2004.

	Shareholders	Shares
Canada	5,863	113,832,462
USA	87	429,192
Others	30	94,011
Total	5,980	114,355,665

Common Shares
December 22, 1971 Closing Price: $3.25[1]
February 22, 1994 Closing Price: $7.75[1]

[1]Adjusted for the two-for-one stock splits on November 18, 1985 and June 3, 2004.

Registrar and Transfer Agent
Shareholder accounts, including dividend payments, direct deposit service and the transfer of shares are handled by the Company's registrar and transfer agent:

CIBC Mellon Trust Company
16th Floor, 1066 West Hastings Street
Vancouver, B.C. V6E 3X1
Telephone: 604-688-4330
Toll-free: 1-800-387-0825
Fax: 604-688-4301
Web site: www.cibcmellon.com

Duplicate Annual and Interim Reports
To eliminate duplicate mailings of annual and quarterly reports, please contact CIBC Mellon Trust Company.

Shares Listed (Symbol: TER)
The Toronto Stock Exchange

Scheduled Dividend Payment Dates
February 28, 2005
May 31, 2005
August 31, 2005
November 30, 2005

Shareholder Relations
Inquiries regarding the Company's Dividend Reinvestment and Share Purchase Plan and all other inquiries or comments by shareholders regarding the Company should be directed to:
Liza Yuzda
Telephone: 604-443-6566
Toll-free (Canada): 1-800-667-9177
Fax: 604-443-6630
E-mail: shareholder@terasen.com

Investor Relations
Portfolio managers, investment analysts and other investors requesting financial information regarding Terasen should contact:
David Bryson
Telephone: 604-443-6527
Fax: 604-443-6673
E-mail: investor.relations@terasen.com

Internet
www.terasen.com

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Terasen Gas
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Surrey, B.C. V3S 2X7
Telephone: 604-576-7000

Terasen Pipelines
#2700, 300 - 5th Avenue SW
Calgary, Alberta T2P 5J2
Telephone: 403-514-6400

Terasen Utility Services
1128 Burdette Street
Richmond, B.C. V6V 2Z3
Telephone: 604-273-4987

Project management: Arlette Communication Inc. Design: Signals Design Group. Printing: Hemlock Printers. Printed on recycled paper.

Terasen

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